No. 7812.

In the United States Circuit Court of Appeals

For the Ninth Circuit.

THE REPUBLIC SUPPLY COMPANY OF CALIFORNIA, a corporation,

Complainant,

vs.

RICHFIELD OIL COMPANY OF CALIFORNIA, a corporation,

Defendant.

SECURITY-FIRST NATIONAL BANK OF LOS ANGELES, as Trustee, GEORGE ARMSBY, F. S. BAER, HARRY J. BAUER, STANTON GRIFFIS, ROBERT E. HUNTER and ALBERT E. VAN COURT, known and designated as Richfield Bondholders' Committee,

Appellants and Cross-Appellees,

vs.

UNIVERSAL CONSOLIDATED OIL COMPANY, a California corporation,

Intervenor, Appellee and Cross-Appellant,

THE CHASE NATIONAL BANK OF THE CITY OF NEW YORK, Receiver for Pan American Petroleum Company, a corporation, BANK OF AMERICA, a corporation, PAN AMERICAN PETROLEUM COMPANY, a corporation, WILLIAM C. McDUFFIE, as Receiver for Pan American Petroleum Company, a corporation, RICHFIELD OIL COMPANY OF CALIFORNIA, a corporation, UNITED STATES OF AMERICA, THE REPUBLIC SUPPLY COMPANY OF CALIFORNIA, a corporation, CITIES SERVICE COMPANY, a corporation, ROBERT C. ADAMS, THOMAS B. EASTLAND, EDWARD F. HAYES, and RICHARD W. MILLAR, known and designated as Pan American Bondholders' Committee, G. PARKER TOMS, ROBERT C. ADAMS, F. S. BAER, ROBERT E. HUNTER, HENRY S. McKEE and RICHARD W. MILLAR,

(Continued on Inside Cover.)

PETITION OF APPELLEE WILLIAM C. McDUFFIE, AS RECEIVER OF RICHFIELD OIL COMPANY OF CALIFORNIA, FOR REHEARING.

Parker, Stone & Baird Co., Law Printers, Los Angeles.

known and designated as Richfield Pan American Reorganization Committee, **WILLIAM C. McDUFFIE**, as Receiver of Richfield Oil Company of California, **SECURITY-FIRST NATIONAL BANK OF LOS ANGELES**, a national banking association, **PACIFIC AMERICAN COMPANY**, a corporation, **AMERICAN COMPANY**, a corporation, **MANUFACTURERS TRUST COMPANY OF NEW YORK**, a corporation, **CITIZENS NATIONAL TRUST & SAVINGS BANK OF LOS ANGELES**, a national banking association, **FIRST NATIONAL BANK AND TRUST COMPANY OF SEATTLE**, a national banking association, **CONTINENTAL ILLINOIS BANK AND TRUST COMPANY**, a corporation, **THE FIRST NATIONAL BANK OF CHICAGO**, a national banking association, **CHEMICAL NATIONAL BANK AND TRUST COMPANY**, a national banking association, and **CALIFORNIA BANK**, a corporation, **M. W. LOWERY, HENRY S. McKEE, O. C. FIELD, R. R. TEMPLETON**, known and designated as Richfield Unsecured Creditors' Committee.

Appellees.

Henry F. Prince,
Homer D. Crotty,
Herbert F. Sturdy,
David P. Evans,
Gibson, Dunn & Crutcher,
By Henry F. Prince,
634 South Spring St., Los Angeles, California,
Solicitors for Appellee, William C. McDuffie, as Receiver of Richfield Oil Company of California.

TOPICAL INDEX.

PAGE

I.

It is respectfully and earnestly submitted that the decision of this court is in error in failing to recognize and apply the basic principles of federal equity receivership established by the United States Supreme Court and by the Circuit Courts of Appeal in other circuits, which may be briefly summed up in the phrase "equality is the highest equity" ... 7

(a) The primary object of a federal equity receivership is to prevent one claimant recovering at the expense of the others, and to bring about a pro rata distribution between claimants. As between claimants "equality is the highest equity" ... 7

(b) There is no preference, priority of "equity" in favor of claimants who become such by reason of fraud as compared with other creditors ... 10

(c) Against the receiver and other creditors of an insolvent trustee, the burden of tracing trust funds into the hands of the receiver is absolutely, continuously and unequivocally on the cestui, and all doubts and possibilities are resolved in favor of the receiver, in order that there may be an equitable, pro rata distribution of the entire estate among all claimants, including the cestui ... 15

(d) The receiver, who is an officer of the court, and the other creditors who have done no wrong to Universal must not be confused with the insolvent tort feasor ... 23

II.

It is respectfully submitted that it is established by the decisions requiring the cestui to prove the "low balance" (Part (a) below), by reason and banking practice (Part (b) below), and by the unanimous authority of five decisions passing directly on the point, two of them affirmed by the United

PAGE

States Supreme Court (Part (c) below). That when a claimant in receivership is seeking to trace trust funds through a commingled account, merely showing the overnight balances of such account is not prima facie or any evidence of the "low balance" of such account. The claimant has the absolute burden of proving the actual "low balance" at all times in the account, and that burden never shifts to the receiver, for to shift it would be to grant an improper preference under the guise of tracing trust funds.. 29

(a) When the low balance theory of tracing is applied to an account in which trust funds and other funds are commingled, the burden is on the cestui to prove the actual low balance continuing in the account at all times between the time the trust funds were commingled in the account and the time to which the cestui is seeking to trace such funds 29

(b) From the standpoint of banking practice and reason, the overnight balances of a bank account are neither prima facie evidence, nor in fact, any evidence at all that the balance in the account did not fall below the closing balance at some time during the preceding day, especially where the amount of checks and deposits entering into the account each day is in evidence.. 33

(c) It is respectfully and earnestly submitted that not only does banking practice, reason and common sense require that the overnight balances be not taken to fix the low balances in the account when the amount of checks and deposits each day are known and in evidence, but that unanimous weight of authority requires that in tracing trust funds against an insolvent estate overnight balances of a bank account be not accepted as prima facie or any evidence of the low balance of the account during the active daytime periods intervening.. 41

PAGE

III.

The Supreme Court of the State of California has established as a rule of property for that state that as against creditors of a trustee ex maleficio the cestui has no interest in a bank account of the trustee in which funds of the cestui and trustee have been commingled after checks to the amount of the cestui's funds in the account have been charged against the account. Under this rule of property and the facts established in this case, Universal had no interest in the Richfield bank account at the time the several investments, which are the subject of this proceeding, were made and consequently could have no interest in the investments. As both the bank account and all of the properties involved are properties in the State of California, and in most cases are interests in real property in the State of California, the above California rule of property should and must be followed by the federal courts 64

IV.

Under the circumstances of this case, when funds of a cestui are commingled in a single bank account with funds of the tort feasor trustee and investments are later made from said bank account, the cestui cannot claim any of such investments at the expense of the other creditors against the trustee's insolvent estate unless the cestui sustains the burden of proving (1) that trust funds remained in the account at the time the investment was made; and (2) that the trust funds so remaining in the account were in fact (and not merely presumptively) appropriated for the purpose of making the particular investment. It is submitted that Universal has not sustained the burden of proof with respect to either of these elements 81

Conclusion 91

TABLE OF AUTHORITIES CITED.

Cases.

PAGE

Acheson Co., In re J. M., 170 Fed. 427....15, 17, 19
Adams v. Champion, 79 L. Ed. Adv. 366....11, 23, 25
American Employers' Inc. Co. v. Maynard, 226 N. W. 686.... 72
Beard v. Independent District of Pella City, 88 Fed. 375.... 74
Bevan v. Citizens National Bank of Lebanon, 19 Ky. Law Rep. 1261.... 82
Blumenfeld v. Union Nat. Bank, 38 Fed. (2) 455....29, 30
Board of Commissioners v. Strawn, 157 Fed. 49....26, 62, 82
Bogena & Williams, In re, 76 Fed. (2) 950....16, 22, 30
Borman et al. v. Sullivan, 77 Fed. (2) 342....29, 31, 32, 36, 42
Brennan v. Tillinghast, 201 Fed. 609.... 86
Bright v. King, 20 Ky. Law Rep. 186.... 82
Brown, In re, 193 Fed. 24....41, 51, 52, 53, 55, 62, 82
Brown & Co., In re, 193 Fed. 30....41, 82, 89, 92
Brown & Co., In re A. O., 189 Fed. 432....41, 48, 50, 82, 85, 90
Brunsing, Tolle & Postel, In re, 169 Fed. 668.... 12
Burnham v. Barth, 62 N. W. 96....36, 82
Byrne, In re, 32 Fed. (2) 189....23, 24, 25
City Bank, In re, 186 Fed. 413.... 82
City of Spokane v. First National Bank of Spokane, 68 Fed. 982.... 82
Clark v. Bacorn, 116 Fed. 617.... 9
Connolly v. Lang, 68 Fed. (2) 199....41, 59
Cook v. Elliott, 73 Fed. (2) 916.... 16
Davis v. Elmira Savings Bank, 161 U. S. 275.... 75
Edward Hines Yellow Pine Trustees v. Martin, 268 U. S. 458, 69 L. Ed. 1050....76, 77
Elmer v. Kemp, 67 Fed. (2d) 948.... 74
Empire State Surety Co. v. Carroll County, 194 Fed. 593.... 82
Farmers' Bank v. Bailey, 221 Ky. 55, 297 S. W. 938.... 27

PAGE

Ferris v. Van Vetcher, 73 N. Y. 113 .... 82, 85
Fiman v. State of South Dakota, 29 Fed. (2) 776 .... 85, 86
First Nat. Bk. of Princeton v. Littlefield, 226 U. S. 110 41
First National Bank of Princeton v. Littlefield, 226 U. S. 110, 57 L. Ed. 145 53
First National Bank of Princeton v. Littlefield, 226 U. S. 110, 57 L. Ed. 145 .... 41, 53, 82
First Nat. Bank of Princeton, Ex parte, A. O. Browne & Co., In re, 189 Fed. 432 .... 41, 47, 82
First Nat. Bk. of St. Petersburg v. City of Miami, 69 Fed. (2) 346 .... 16, 21
Gianella v. Momsen, 63 N. W. 1018 82
Grand Forks County v. Baird, 54 N. Dak. 315, 209 N. W. 782 27
Gunter v. Janes, 9 Cal. 643 65
Harmer v. Rendleman, 64 Fed. (2) 422 .... 16, 20
Harry E. Jones, Inc. v. Kemp, 74 Fed. (2) 623 .... 23, 24
Hawaiian Pineapple Co. v. Browne, 69 Mont. 140, 220 Pac. 1114 27
Israel v. Woodruff, 299 Fed. 454 27
Jennings v. U. S. Fidelity & Guaranty Co., 79 L. Ed. Adv. 355 63
John Deere Plow Co. v. McDavid, 137 Fed. 802 74
Jones v. Harrison, 7 Fed. (2) 461; 270 U. S. 652 76
Jones v. Harrison, 7 Fed. (2d) 461, certiorari denied; 270 U. S. 652 80
Jones v. Readey, 270 U. S. 652 80
Kershaw v. Jenkins, 71 Fed. (2) 647 .... 16, 29, 30
Knatchbull v. Hallett, 13 Ch. Div. 696 .... 65, 71
Lathrop v. Bampton, 31 Cal. 17 12
Lincoln v. First National Bank of Cadiz, 172 U. S. 425 75
Lucas County v. Jamison, 170 Fed. 338 12
Marshburn v. Williams, 15 Fed. (2) 589 .... 41, 42, 44
Maryland Casualty Co. v. Williams, 159 So. 242 .... 23, 25, 26
Matthews' Sons, Inc., In re A. D., 238 Fed. 785 .... 16, 20

PAGE

Merchants & Farmers Bank v. Austin, 48 Fed. 25 12
Meyers v. Baylor University, 6 S. W. (2) 393 27
Mitchell v. Dunn, 211 Cal. 129 ....64, 71
Moore v. Jones, 63 Cal. 12 85
Mulligan, In re, 116 Fed. 715 ....30, 63, 75
Multnomah County v. Oregon Nat. Bank, 61 Fed. 912....12, 14, 36
National Bank v. Insurance Co., 104 U. S. 54 ....35, 65
Nixon State Bank v. First State Bank of Bridgeport, 60 So. 868 ....41, 45, 47
Noble v. Noble, 198 Cal. 129 74
Oatway, In re, 2 Ch. Div. 356 ....86, 88
Orcutt v. Gould, 117 Cal. 315 30
Pacat Finance Corp., 27 Fed. (2) 810 85
People v. California Safe Deposit & Trust Co., 175 Cal. 756.... 66
Peters v. Bain, 133 U. S. 670 ....82, 83
Philadelphia Nat'l Bank v. Dowd, 38 Fed. 172 72
Pickens v. Merriam, 274 Fed. 1 ....76, 78
Poole v. Elliott, 76 Fed. (2) 772 ....16, 72
Porter v. Boyd, 171 Fed. 305 9
Pottorff v. Key, 67 Fed. (2) 833 ....11, 12
Primeau v. Granfield, 184 Fed. 480 ....47, 54, 85
Rugger v. Hammond, 163 Pac. 408 72
Scandinavian-American Bank v. Sabin, 227 Fed. 579 ....76, 78
Schuyler v. Littlefield, 232 U. S. 707, 58 L. Ed. 806 ....15, 16, 17, 18, 41, 89, 90, 93
Schuyler, Chadwick & Burnham, Ex parte, A. O. Browne & Co., In re, 189 Fed. 432 ....41, 54, 82
S. L. & S. F. R. Co. v. Spiller, 274 U. S. 304 20
Slater v. Oriental Mills, 18 R. I. 352, 27 Atl. 443 ....11, 13
Smith v. Mottley, 150 Fed. 266 61
Standish v. Babcock, 50 N. J. Eq. 628 82

PAGE

Stilson v. First State Bank, 129 N. W. 70..........12, 70

First Nat. Bk. of Princeton v. Littlefield, 226 U. S. 110......41, 82

Taylor v. Morris, 163 Cal. 717.......... 85

Texas & Pac. Ry. Co. v. Pottorff, Rec'r, 291 U. S. 245, 78 L. Ed. 777, 786, note 19..........11, 13, 15, 17

Titlow v. McCormick, 236 Fed. 209..........15, 17, 18, 93

United States v. Pan American Petroleum Company, 55 Fed. (2) 753.......... 10

Wisdom v. Keen, 69 Fed. (2) 349..........11, 23

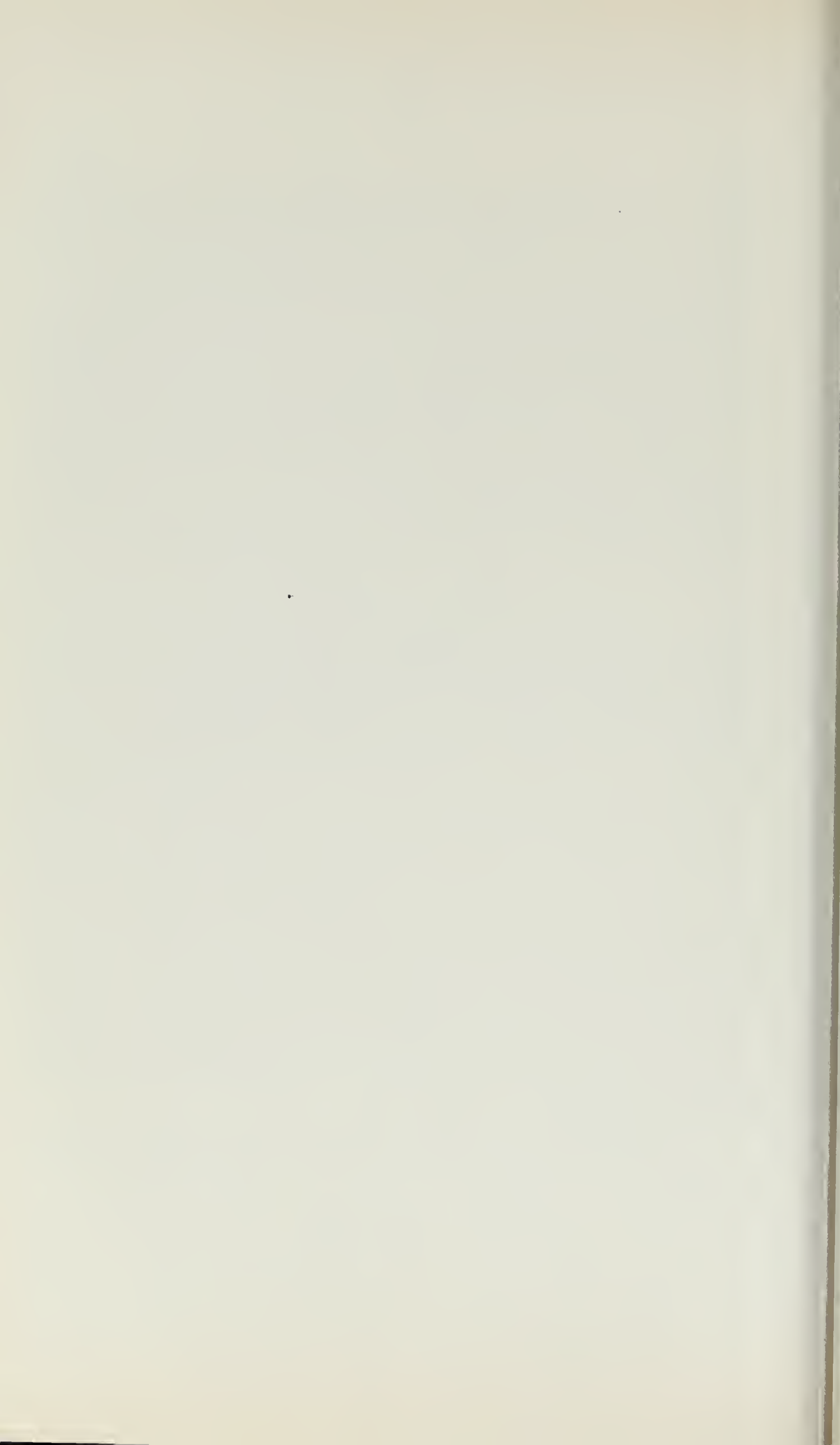
Wisdom v. Keen, 69 Fed. (2) 349.......... 11

TEXT BOOKS AND ENCYCLOPEDIAS.

1 Bowles, Modern Law of Banking, p. 190..........12, 15

Hughes Federal Practice, vol. 6, sec. 3712, p. 238-9.......... 76

Hughes, Federal Practice, vol. 6, sec. 3715, p. 248.......... 78



In the United States
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THE REPUBLIC SUPPLY COMPANY OF CALIFORNIA, a corporation,

Complainant,

vs.

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Defendant.

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Appellants and Cross-Appellees,

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Intervenor, Appellee and Cross-Appellant,

THE CHASE NATIONAL BANK OF THE CITY OF NEW YORK, Receiver for Pan American Petroleum Company, a corporation, BANK OF AMERICA, a corporation, PAN AMERICAN PETROLEUM COMPANY, a corporation, WILLIAM C. McDUFFIE, as Receiver for Pan American Petroleum Company, a corporation, RICHFIELD OIL COMPANY OF CALIFORNIA, a corporation, UNITED STATES OF AMERICA, THE REPUBLIC SUPPLY COMPANY OF CALIFORNIA, a corporation, CITIES SERVICE COMPANY, a corporation, ROBERT C. ADAMS, THOMAS B. EASTLAND, EDWARD F. HAYES, and RICHARD W. MILLAR, known and designated as Pan American Bondholders' Committee, G. PARKER TOMS, ROBERT C. ADAMS, F. S. BAER, ROBERT E. HUNTER, HENRY S. McKEE and RICHARD W. MILLAR, known and designated as Richfield Pan American Reorganization Committee, WILLIAM C. McDUFFIE, as Receiver of Richfield Oil Company of California, SECURITY-FIRST NATIONAL BANK OF LOS ANGELES, a national banking association, PACIFIC AMERICAN COMPANY, a corporation, AMERICAN COMPANY, a corporation, MANUFACTURERS TRUST COMPANY OF NEW YORK, a corporation, CITIZENS NATIONAL TRUST & SAVINGS BANK OF LOS ANGELES, a national banking association, FIRST NATIONAL BANK AND TRUST COMPANY OF SEATTLE, a national banking association, CONTINENTAL ILLINOIS BANK AND TRUST COMPANY, a corporation, THE FIRST NATIONAL BANK OF CHICAGO, a national banking association, CHEMICAL NATIONAL BANK AND TRUST COMPANY, a national banking association, and CALIFORNIA BANK, a corporation, M. W. LOWERY, HENRY S. McKEE, O. C. FIELD, R. R. TEMPLETON, known and designated as Richfield Unsecured Creditors' Committee.

Appellees.

PETITION OF APPELLEE WILLIAM C. McDUFFIE, AS RECEIVER OF RICHFIELD OIL COMPANY OF CALIFORNIA, FOR REHEARING.

To the Honorable United States Circuit Court of Appeals for the Ninth Circuit, and the Judges Thereof:

Appellee, William C. McDuffie, as Receiver of Richfield Oil Company of California, representing as he does the more than six thousand persons who filed claims in the receivership of Richfield, respectfully but earnestly petitions for a rehearing of said cause by this Court on the bill in intervention and claim of Universal Consolidated Oil Company upon all of the grounds hereinafter set forth.

In support of this petition we respectfully submit that the decision which this Court has rendered in the pending cause is erroneous in each of the matters below specified.

1. It fails to recognize and give effect to the well established basic rules in equity receiverships (a) that the primary object of such receiverships is to bring about a *pro rata* distribution between claimants, and that as between claimants "equality is the highest equity," (b) that there is no preference, priority or "equity" in favor of claimants who become such by reason of fraud as compared with other creditors, (c) that a fraud claimant participates in the estate *pro rata*, solely as a general creditor, unless such fraud claimant has sustained with evidence the burden of absolutely identifying his property or its substitute in the hands of the receiver, with every doubt

or possibility resolved in favor of the receiver, in order that equality of distribution may be preserved, and (d) that the receiver, who is an officer of the court, and the other creditors who have done no wrong to the fraud claimant, must not be confused with the insolvent tort feasor.

2. It fails to recognize and give effect to the rule established by reason, banking practice, *and the unanimous authority of five decisions passing directly on the point,* two of them affirmed by the United States Supreme Court, to the effect that when a claimant in receivership is seeking to trace trust funds through a commingled account, merely showing the overnight balances of such account is not *prima facic* or *any* evidence of the "low balance" of such account. The claimant has the absolute burden of proving the actual "low balance" at all times remaining in the account, and that burden never shifts to the receiver, for to shift it would be to grant *an improper preference* under the guise of tracing trust funds. We appreciate that the failure of this Court to give effect to these decisions was due to the fact that most of them were not cited to the Court by counsel for Security-First National Bank of Los Angeles (herein referred to as the Richfield bond trustee), and to the further fact that counsel for the Richfield bond trustee did not emphasize those of the decisions which were cited.

3. It fails to recognize and apply the local rules of property established by the decisions of the Supreme Court of the State of California with respect to the prop-

erties which are the subject of these proceedings, all of which are either real or personal property situated in the State of California. The Supreme Court of the State of California has established the rule of property that as against creditors of an insolvent trustee *ex maleficio,* a *cestui* claimant has no property interest in a bank account of the trustee in which funds of the *cestui* and trustee have been commingled, once checks equal in amount to the *cestui's* funds deposited in the account have been charged against that account. It is respectfully but earnestly submitted that this rule of property is binding on the federal courts, and that under this rule and the facts established in this case, Universal had no property interest in the Richfield bank account at the time the several investments, which are the subject of this proceeding, were made, and consequently could not possibly have a property interest in the investments.

4. It is contrary to the weight of authority, the decisions of the United States Supreme Court, and the decisions in other circuits, in that it permits "tracing" of trust funds from a commingled account into investments made with checks against that account, without any evidence whatsoever that the trust funds were in fact appropriated to the investments. There is no requirement that the trust funds must be traced into the identical dollars deposited or that the trust funds can only be traced into money, but the overwhelming weight of authority is to the effect that to trace trust funds from a commingled account into an investment there must be evidence that the trust funds in the account were in fact appropriated to the particular investment into which it is sought to trace them.

I.

It Is Respectfully and Earnestly Submitted That the Decision of This Court Is in Error in Failing to Recognize and Apply the Basic Principles of Federal Equity Receivership Established by the United States Supreme Court and by the Circuit Courts of Appeal in Other Circuits, Which May Be Briefly Summed Up in the Phrase "Equality Is the Highest Equity".

While the discussion of this first point is divided for convenience into four parts, it will be obvious to the Court that the decisions cited in each of the four parts have a direct bearing one upon the other, and should be considered together. With this thought in view we will not burden the Court by repeating the citation of a case under each part to which it may be relevant.

(a) The Primary Object of a Federal Equity Receivership Is to Prevent One Claimant Recovering at the Expense of the Others, and to Bring About a Pro Rata Distribution Between Claimants. As Between Claimants "Equality Is the Highest Equity."

The Receiver holds no brief for, and in no wise champions, Richfield or its former officers. Richfield is defunct, its chief former officers are now or have been incarcerated, and the Receiver has done what he could to assist in bringing them to justice and in collecting for the creditors on their bonds. The Receiver is all too aware of the hardships which Richfield's acts and subsequent failure impose on Universal—and on each of the other some six thousand claimants against the estate. In certain instances the economic hardship caused by the Rich-

field receivership on claimants was so unbearable that the taking of their lives can be traced to the Richfield failure. Richfield was legally, equitably and morally bound to have repaid them *all* in full. Financial failure has made that impossible and the Federal Courts have appointed the Receiver as an officer of the Court to take over the assets of Richfield in order that there may be an equitable pro-rated distribution of the proceeds of those assets among all claimants, rather than the estate torn apart for the benefit of certain claimants at the expense of the rest.

An apparent exception to the rule of equality is that if a claimant can in fact establish that certain property held by the Court is the claimant's property and not part of the receivership at all, the Court will return his property to him. While the courts recognize that they would not be justified in dividing up among all claimants, as a part of the receivership estate, property in the hands of the receiver which one claimant was in fact able to prove was his own property, nevertheless it is equally well established that if any claimant to assets fails to absolutely identify and prove them as his own, as for example "where the means of ascertainment fail" or where evidence is such that the property may or may not be that of the claimant, the courts regard it as the highest equity to leave the property in the receivership estate for *pro rata* distribution to all claimants, including the claimant who seeks to trace, rather than take a chance on granting an unwarranted preference to one claimant at the expense of the rest. It is respectfully submitted that the decision of this Court in the above entitled cause is in error in holding that where, under the evidence, the property in question may or may not be that of the claimant who seeks to trace, and where, as here, the means of

ascertainment of the facts which would determine whether or not the property in question is that of the claimant have failed, the court should take the property out of the receivership estate and give it to one creditor at the expense of the others, even though the very purpose of the equity receivership was to insure a *pro rata* distribution and prevent preferences. As said by this Honorable Court in *Clark v. Bacorn* (C. C. A. 9, 1902), 116 Fed. 617-618:

> "It is well settled that when a corporation becomes insolvent, and the corporate assets have passed into the hands of a receiver, such assets constitute a fund for ratable distribution among its creditors. * * *" *Clark v. Bacorn,* 116 Fed. 617-618.

As stated in *Porter v. Boyd* (C. C. A. 3, 1909), 171 Fed. 305, 313:

> "* * * the rule of equity requires the *pro rata* division of the assets among the creditors, subject to the allowance of costs and expenses and the adjustment and liquidation of priorities and preferences. *Equality* or a *pro rata* distribution of the assets among the creditors *being the most equitable result attainable,* no liens or preferences should be recognized *unless satisfactorily established;* and it is not only proper, but it is incumbent upon the receiver to protect the funds or assets in his hands against all attempts of creditors to defeat equality of distribution." *Porter v. Boyd,* 171 Fed. 305, 313.

Among the some six thousand claimants who have presented their claims to the Federal Courts, relying on these courts to make an equitable *pro rata* distribution among them, are many whose claims are based on fraud equally

as reprehensible as that in the case of Universal, if not more so. This Court need only recall the judgment allowed by this Court in *United States v. Pan American Petroleum Company,* 55 Fed. (2) 753, for stolen oil from the Naval Petroleum Reserve, considerable portions of which oil were traced to Richfield from its subsidiary, Pan American Petroleum Company. This proceeding is not like a single issue between two rival claimants, for here allowing a preference to one will be at the expense of the rest, many of whom undoubtedly have claims even more appealing to the sympathy than Universal.

(b) There Is No Preference, Priority of "Equity" in Favor of Claimants Who Become Such by Reason of Fraud as Compared With Other Creditors.

In its opinion the Court expresses the thought that Universal has a greater "equity" than other creditors. If Universal had succeeded in tracing title to certain properties they would have established an equity or interest in those properties. But it is submitted that prior to establishing their title or interest in properties in the estate, Universal is entitled to no "equity", consideration, or preference over other claimants against the estate. To dispense with evidence proving title, or to resolve doubt as to the tracing of title in favor of Universal, or to shift the burden of proof of tracing to the Receiver, is merely to grant an improper preference under the guise of tracing. It is doing indirectly what the courts have repeatedly decided they would not do directly, to-wit, "allowing a *cestui* arbitrary preference because of the hardships and sympathies connected with his plight."

There are three types of claims in a receivership action such as that of Richfield: (a) general unsecured claims,

(b) preferred claims, (c) claims to a lien upon or title to specific items of property in the possession of the court. In those cases where a trust is raised by reason of conversion or misappropriation of funds, and the trustee *ex maleficio* becomes insolvent and a receiver is appointed, there is an equitable attachment of all of the property for prorated distribution to all creditors, including the defrauded *cestui* except to the extent that the *cestui* clearly identifies items of property in the receiver's hands as being the *cestui's* property and therefore not part of the receivership estate at all. With respect to the status of the *cestui* as a claimant, both the Federal Courts and the courts of California have repeatedly considered the hardships upon and the sympathies for a *cestui* claimant and have firmly established the rule that such hardships and sympathies do not entitle the *cestui* claimant to any preference or consideration over other claimants to the insolvent estate. With respect to the *cestui* as a claimant of an identified trust *res,* his rights are property rights which he must establish by clear and unequivocable proof according to the rules for tracing titles.

> *Pottorff v. Key* (C. C. A. 5, 1933), 67 Fed. (2) 833;
>
> *Texas & Pac. Ry. Co. v. Pottorff, Receiver* (1934), 291 U. S. 245, 261;
>
> *Slater v. Oriental Mills* (1893), 18 R. I. 352, 27 Atl. 443;
>
> *Wisdom v. Keen* (C. C. A. 5, 1934), 69 Fed. (2) 349 (cited with approval in Adams v. Champion, (1935), 79 L. Ed. Adv. 366, 369);
>
> *Swan v. Children's Home Society of West Virginia* (C. C. A. 4, 1933), 67 Fed. (2) 84, 88; Cert. denied, 290 U. S. 704, 78 L. Ed. 605;

Multnomah County v. Oregon Nat. Bank (C. C. Ore. 1894), 61 Fed. 912, 914;

In re Brunsing, Tolle & Postel (D. C. Cal. 1909), 169 Fed. 668, 669;

Lathrop v. Bampton (1866), 31 Cal. 17, 23-24;

Merchants & Farmers Bank v. Austin (C. C. Ala. 1891), 48 Fed. 25, 32;

Lucas County v. Jamison (C. C. Ia., 1908), 170 Fed. 338, 348-349;

Stilson v. First State Bank (1910 Ia.), 129 N. W. 70, 72-73;

1 *Bowles, Modern Law of Banking,* p. 190.

It is respectfully submitted that the decision in the instant case in this regard is at variance with the decisions of the United States Supreme Court, and with the decisions of the other circuit courts of appeal.

In *Pottorff v. Key* (C. C. A. 5 1933), 67 Fed. (2) 833, 834, the court said of a *cestui* who had failed to trace his money into the funds coming to the receiver's hand:

> "Though the victim of a wrong and an involuntary creditor, *he has for that reason no better equitable right to what is in the receiver's hands than other creditors have.* The contrary view expressed in San Diego County v. California Nat'l Bank (C. C.), 52 F. 59, was disapproved in Multonomah County v. Oregon Nat'l Bank (C. C.), 61 F. 912, and Spokane County v. First Nat'l Bank (C. C. A.), 68 F. 979, and we believe *has not since been asserted in the federal courts.*" (Italics ours.) *Pottorff v. Key,* 67 Fed. (2) 833, 834.

In *Texas & Pac. Ry. Co. v. Pottorff, Receiver* (1934), 291 U. S. 245, 261, the United States Supreme Court said that a claim of unjust enrichment when a receiver sets aside a pledge as *ultra vires*

> "does not, in the absence of an *identifiable res*[19] and a constructive trust based on special circumstances of misconduct, confer a preference over other creditors."

The Court's Note 19 on page 261 says:

> *"The claimant has the burden of identifying the property in its original or altered form. Schuyler v. Littlefield,* 232 U. S. 707, 58 L. Ed. 806, 34 S. Ct. 466 * * *." (Italics ours.) *Texas & Pacific Ry. Co. v. Pottorff, Receiver* (1934), 291 U. S. 245, 261.

The case of *Slater v. Oriental Mills,* 18 R. I. 352, 27 Atl. 443 (1893), used the following language which has been many times cited and approved by both Federal and State courts:

> "Undoubtedly, it is right that everyone should have his own; but when a claimant's property cannot be found, this same principle prevents the taking of property which equitably belongs to creditors of the trustee to make it up. The creditors have done no wrongful act, and should not be called upon, in any way, to atone for the misconduct of their debtor. It is an ordinary case of misfortune on the part of claimants, whose confidence in a trustee or agent has been abused." *Slater v. Oriental Mills,* 18 R. I. 352, 27 Atl. 443.

In *Swan v. Children's Home Society of West Virginia* (C. C. A. 4, 1933), 67 Fed. (2) 84, 88 (Cert. denied 290 U. S. 704, 78 L. Ed. 605), funds had been left to an

orphans' home and were left with a trustee bank, which failed. The Court denied a preference, saying:

> "Those entitled to trust funds held by the bank may enforce the trust against the receiver, not on the ground that the law gives them a preferred status, but that the receiver has property which in equity and good conscience belongs to them. But, unless they can trace the trust funds into some fund or specific property which has come into his hands, or can show that the assets in his hands have been directly augmented as a result of the conversion of the trust funds by the bank, they have no basis upon which relief can be granted them. * * *
>
> We can think of no nobler charity, nor of one making a stronger appeal to the human heart, than that of the plaintiff here, engaged as it is in providing for orphan and homeless children; and it is most unfortunate that funds intended for its use should have been lost. We have no option, however, but to declare the law as we find it." *Swan v. Children's Home Soc. of West Virginia,* 67 Fed. (2) 84, 88.

In *Multnomah County v. Oregon Nat. Bank* (C. C. Ore. 1894), 61 Fed. 912, 914, the court said:

> "The fact that the money of such creditor or *cestui que trust* cannot be traced to the fund sought to be charged is the reason that the preference is refused. * * * *His so-called right of preference, in other words, cannot in justice extend to the property of others. The theory of preference does not apply in these cases. There is no preference by reason of an unlawful conversion.* * * * When the means of ascertainment of the identity of property or proceeds fail, the right fails." *Multnomah County v. Oregon Nat'l Bank,* 61 Fed. 912, 914.

1 *Bowles, Modern Law of Banking,* page 190, states:

> "Many a beneficiary has been unable to recover, not through his failure to prove the existence of a trust, but of a fund that he could rightfully claim as his own."

(c) Against the Receiver and Other Creditors of an Insolvent Trustee, the Burden of Tracing Trust Funds Into the Hands of the Receiver Is Absolutely, Continuously and Unequivocably on the Cestui, and All Doubts and Possibilities Are Resolved in Favor of the Receiver, in Order That there May Be an Equitable, Pro Rata Distribution of the Entire Estate Among All Claimants, Including the Cestui.

If the trust fund is not clearly identified at all times between its creation and the advent of receivership, as for instance in a case where the means of ascertainment fail for lack of records, the equitable principle of equality places the *cestui* on a parity with other creditors to share ratably in the whole receivership estate, including the properties sought to be traced. The whole reason for receiverships and the unanimous weight of authority in the decided cases require that all doubts as to identification be resolved against the claimant.

Schuyler v. Littlefield (1914), 232 U. S. 707, 713, 58 L. Ed. 806, 809;

Texas & Pac. Ry. Co. v. Pottorff, Rec'r (1934), 291 U. S. 245, 261, 78 L. Ed. 777, 786, note 19;

Titlow v. McCormick (C. C. A. 9, 1916), 236 Fed. 209, 211;

In re J. M. Acheson Co. (C. C. A. 9, 1909), 170 Fed. 427;

Poole v. Elliott (C. C. A. 4, 1935), 76 Fed. (2) 772, 774;

In re A. D. Matthews' Sons, Inc. (C. C. A. 2, 1916), 238 Fed. 785, 786;

Cook v. Elliott (C. C. A. 4, 1934), 73 Fed. (2) 916, 918;

Harmer v. Rendleman (C. C. A. 4, 1933), 64 Fed. (2) 422, 423;

First Nat. Bk. of St. Petersburg v. City of Miami (C. C. A. 5, 1934), 69 Fed. (2) 346, 349;

Kershaw v. Jenkins (C. C. A. 10, 1934), 71 Fed. (2) 647, 649;

In re Bogena & Williams (C. C. A. 7, 1935), 76 Fed. (2) 950, 955.

The decision in the instant case in this regard is clearly at variance with prior decisions of the United States Supreme Court and with the decisions of the other Circuit Courts of Appeal.

In the case of *Schuyler v. Littlefield,* 232 U. S. 707, 713, 58 L. Ed. 806, 809 (1914), the court said:

> "They were practically asserting title to $9,600, said to have been traced into stock in the possession of the trustee. Like all other persons similarly situated, they were under the burden of proving their title. *If they were unable to carry the burden of identifying the fund* as representing the proceeds of their interborough stock, *their claim must fail. If their evidence* left the matter of identification *in doubt,* the doubt must be resolved *in favor of the trustee,* who represents all of the creditors * * *, some of whom appear to have suffered in the same way. Like them, the appellant must be remitted to the general fund." (Italics ours.) *Schuyler v. Littlefield,* 232 U. S. 707, 713, 58 L. Ed. 806, 809.

In *Texas & Pac. Ry. Co. v. Pottorff, Receiver* (1934), 291 U. S. 245, 261, the court repeated its earlier decision that where a *cestui* seeks to trace a trust *res* into the hands of a receiver

> *"the claimant has the burden of identifying the property in its original or altered form." Texas & Pac. Ry. Co. v. Pottorff, Rec'r,* 291 U. S. 245, 261, note 19.

In *Titlow v. McCormick* (C. C. A. 9), 236 Fed. 209, 211, this Court, through Ross C. J., said:

> "In Schuyler v. Littlefield, Trustee of Brown & Co., 232 U. S. 707, 34 Sup. Ct. 466, 58 L. Ed. 806, it was *distinctly* adjudged by the Supreme Court that where one has deposited trust funds in his individual bank account, and the mingled fund is at any time wholly depleted, the trust fund is thereby dissipated, and cannot be treated as reappearing in sums subsequently deposited to the credit of the same account. It was in that case further *adjudged,* as it has been in many others, that one seeking to charge a fund in the hands of a trustee for the benefit of all creditors as being the proceeds of his property, and therefore a special trust fund for him, has the burden of proof, and if he is unable to identify the fund as representing the proceeds of his property, his claim must fail, *as all doubt must be resolved in favor of the trustee who represents all creditors.* This court also so held in the case of *In re* J. M. Acheson Co., 170 Fed. 427, 95 C. C. A. 597." (Italics ours.) *Titlow v. McCormick,* 236 Fed. 209, 211.

In his brief *amicus curiae* Mr. David R. Faries cites *In re J. M. Acheson Co.* (C. C. A. 9), 1909, 170 Fed. 427, as indicating that there is some burden of proof on the Receiver. (*Amicus curiae* brief, page 15.) The *Acheson*

case was decided before *Schuyler v. Littlefield;* it was construed by this Court in *Titlow v. McCormick, supra,* to hold that all doubts must be resolved in favor of the trustee in bankruptcy; and Mr. Faries quotes only an isolated portion of the opinion which the Court later expressly construes against Mr. Faries' contention. The *Acheson* case was disposed of entirely on a demurrer to the complainant's complaint seeking to trace trust funds. The Court commented upon the fact that the complaint alleged that trust funds were mingled with the trustee's own funds, and that the trustee then "used *the said trust funds* to pay its current running expenses, its creditors other than petitioner, and to buy merchandise, which merchandise composed the bankrupt's assets which passed into the hands of the Receiver of the Court and were sold by him".

As quoted by Mr. Faries, the court said:

> "In carrying out the rule, when it comes to proof, *the owner must assume the burden of ascertaining and tracing the trust funds,* showing that the assets which have come *into the hands of the trustee* have been directly added to or benefited by an amount of money realized from the sales of the specific goods held in trust; and recovery is limited to the extent of this increase or benefit. City Bank of Hopkinsville v. Blackmore, 75 Fed. 771, 21 C. C. A. 514; Cushman v. Goodwin, 95 Me. 353, 50 Atl. 50. If, however, he succeeds in making requisite proof, it then devolves upon the bankrupt, or the trustee who takes the property of the bankrupt, in the same relation that it was held by the bankrupt, to distinguish between what is his and that of the *cestui que trust.* Smith v. Mottley, 150 Fed. 266, 80 C. C. A. 154;

Smith v. Township of Au Gres, 150 Fed. 257, 80 C. C. A. 145, 9 L. R. A. (N. S.) 876." *In re J. M. Acheson Co.,* 170 Fed. 427, 429.

As Mr. Faries failed to quote, the court said:

"We do not mean to be understood as holding that equity will grant to a *cestui que trust* relief against any assets in the hands of a trustee, for it will not go farther than to give a lien *when the facts are* that there *remain in the estate* specific funds or property which have increased the assets of the estate, and which represent the proceeds of the specific property intrusted to the bankrupt. Lowe v. Jones, Adm'r, 192 Mass. 94, 78 N. E. 402, 6 L. R. A. (N. S.) 487, 116 Am. St. Rep. 225. Moreover, if there has been expenditure, and the funds are gone, and no specific property or money is found instead of the funds *it is inequitable that some other property found should be applied to pay one creditor in preference to another.* So, funds that have been dissipated or that have been used to pay other creditors or that have been spent to pay current business expenses are not recoverable, because they are gone and there is nothing remaining to be the subject of the trust. This qualification of the general rule is to be applied to the facts pleaded in the present case inasmuch as it is alleged that some of the trust moneys were used by the bankrupt in paying its employes, and in the expenses of running its business, and in paying other creditors. For them there can be no recovery. Slater *et al.* v. Oriental Mills *et al.,* 18 R. I. 352, 27 Atl. 443; Nototuck Silk Co. v. Flanders, 87 Wis. 237, 58 N. W. 383. But for the moneys represented by assets which went into the hands of the receiver under the circumstances alleged, and which the petition charges that the receiver had when claimants filed their petition,

there appears to be an equitable claim, to support which *petitioners should be allowed to introduce evidence.*" (Italics ours.) *In re J. M. Acheson Co.*, 170 Fed. 427, 430.

In the case of *In re A. D. Matthews' Sons, Inc.* (C. C. A. 2, 1916), 238 Fed. 785, 786 (approved in *S. L. & S. F. R. Co. v. Spiller,* 274 U. S. 304, 310), when a department store failed, one who had conducted a department under an agreement that funds from his department would be kept separate, endeavored to reclaim his funds. The Court held there was no tracing, saying:

> "* * * the burden of proof was upon the fashion company to clearly trace the proceeds of said sales into 'some specific fund or property' in the hands of the trustee in bankruptcy (*In re* McIntyre, 185 Fed. 96, 108 C. C. A. 543; *In re* Ennis, 187 Fed. 728, 109 C. C. A. 476; *In re* Brown, 193 Fed. 24, 113 C. C. A. 348, affirmed as Schuyler v. Littlefield, 232 U. S. 707, 34 Sup. Ct. 466, 58 L. Ed. 806; *In re* See, 209 Fed. 174, 126 C. C. A. 120); and if petitioner did not succeed in carrying that burden of identification, *if the evidence left the matter in doubt, such doubt must be resolved in favor of the trustee.*" (Italics ours.) *In re A. D. Matthews' Sons, Inc.*, 238 Fed. 785, 786.

The decision in *Harmer v. Rendleman* (C. C. A. 4, 1933), 64 Fed. (2d) 422, 423, was by Judge Parker, who, as will later appear, decided a great number of trust fund tracing cases in West Virginia. The court said:

> "The old rule with regard to the tracing of trust funds wrongfully misapplied, or the proceeds of property wrongfully converted, was that the right ceased

> when the property was turned into money and mixed and confounded in the general mass of property of the same description. * * * The modern rule, however, is that where such property or its proceeds has gone to swell the aggregate in the possession of the fraudulent party, it may, under proper proceedings, be segregated in amount from such aggregate sum, and made the subject of a trust, in order to accomplish the ends of justice. * * *
>
> *But there is a limitation upon this modern rule as well settled as the rule itself,* viz., that it is not sufficient to prove merely that the trust property has gone into the general estate and has presumably increased its amount and value. It is *indispensable that clear proof be made* that the trust property or its proceeds has gone into a specific fund, or into a specific identified piece of property, or has directly augmented a fund upon which the trust is to be declared. When it is sought to impress funds in the hands of a receiver with a trust on account of the wrongful conversion of trust property by an individual or corporation to whose rights he has succeeded, *it must be shown* that the funds in his hands have been directly augmented by the presence of the trust property or its proceeds, so that a court of equity can see *with certainty* that the trust property *is in his hands.*" (Italics ours.) *Harmer v. Rendleman,* 64 Fed. (2) 422, 423.

In *First Nat. Bank of St. Petersburg v. City of Miami* (C. C. A. 5 1934), 69 Fed. (2) 346, 349, the court denied the claim of a *cestui* who sought to impress a trust on funds in the hands of a receiver, saying:

> "* * * to obtain preferential treatment in the distribution of the assets of failed banks, one seeking

> to charge the fund in the hands of the receiver for the benefit of all the creditors, as being his property or its proceeds, *has a heavy burden of proof,* and unless he clearly and certainly identifies the fund he must fail. Schuyler v. Littlefield, 232 U. S. 707, 34 S. Ct. 466, 58 L. Ed. 806. We do not understand anything decided in the Miami Bank Case, *supra,* contravenes these views. Any expression in it, which admits of a contrary construction, is expressly disapproved." (Italics ours.) *First Nat. Bk. of St. Petersburg v. City of Miami,* 69 Fed. (2) 346, 349.

In the case of *In re Bogena & Williams* (C. C. A. 7 1935), 76 Fed. (2) 950, 955, the court summed up the tendency in recent United States Supreme Court and Circuit Court of Appeals cases as follows:

> "We do not wish to be understood as saying that the recent decisions have abrogated former positive rules of law with respect to trust funds, *but they have required stricter proof in the establishment of trust funds where general creditors are involved.*" (Italics ours.) *In re Bogena & Williams,* 76 Fed. (2) 950, 955.

We respectfully submit that the opinion of this Court is at variance with the foregoing decision of the United States Supreme Court and of the other Circuit Courts of Appeal in that it places the burden of proof *on the receiver* with respect to one of the essential facts necessary to the tracing of Universal's funds, a fact of which the means of ascertainment have now failed. The decision of this Court in effect dispenses with proof of tracing, for until the chain of evidence is completed there is no tracing at all. A "partial" tracing is in effect nothing more than an improper preference.

(d) The Receiver, Who Is an Officer of the Court, and the Other Creditors Who Have Done No Wrong to Universal Must Not Be Confused With the Insolvent Tort Feasor.

We respectfully submit that this Court was in error in assuming that Universal's claim in the receivership is to be regarded in the same light as had it been against the tortfeasor Richfield. In the opinion it is stated that it was admitted that the Receiver was a constructive trustee for Universal. Rather, the admission was that Richfield was the constructive trustee for Universal. The Receiver made no admission and expressly denies that any such trust relationship existed between himself and Universal. Again, it is stated later in the opinion, with respect to the dearth of evidence on the low balance, "Such liability as might have resulted therefrom should be borne by the tortfeasor, not the innocent *cestui*." It is submitted that the tortfeasor Richfield has no further interest in this matter. Any issue now is between the many claimants against the receivership estate, including Universal. We respectfully protest confusing the Receiver with the tortfeasor Richfield in these proceedings.

Harry E. Jones, Inc. v. Kemp (C. C. A. 9, 1935), 74 Fed. (2) 623, 627;

In re Byrne (C. C. A. 2, 1929), 32 Fed. (2) 189, 190;

Wisdom v. Keen (C. C. A. 5, 1934), 69 Fed. (2) 349 (cited with approval in *Adams v. Champion*, 79 L. Ed. Adv. 366, 369);

Maryland Casualty Co. v. Williams (Ala., 1935), 159 So. 242, 244.

In the case of *Harry E. Jones, Inc. v. Kemp* (C. C. A. 9, 1935), 74 Fed. (2) 623, 627, the claimants of a trust against an insolvent estate asserted that the receiver was estopped to show that the bank accounts into which their funds went had been dissipated. The court denied this, saying:

> "The contention that the receiver 'stands in the same position that the Guaranty Building and Loan Association does,' and therefore 'is estopped to show the moneys received from Investors of America and H. E. Jones, Inc., is not on hand,' is without meat. It is an admitted fact that the association was insolvent when the assets were taken over by the receiver. Under such circumstances the receiver is not only bound to consider rights of claimants as between such claimants and the insolvent corporation, but the respective rights of creditors as between themselves." *Harry E. Jones, Inc. v. Kemp* (C. C. A. 9, 1935), 74 Fed. (2) 623, 627.

In the case of *In re Byrne* (C. C. A. 2, 1929), 32 Fed. (2) 189, 190, cliamants showed that certain securities were turned over to a broker which he was to hold in trust but instead converted. Upon the bankruptcy of such broker claimants seek a preference against the bankruptcy estate. This was denied, the court saying:

> "The appellants have quite misapprehended their rights and have proceeded throughout on the assumption that they are entitled to the same relief in bankruptcy as they would have had against the bankrupts

in personam. Their claim is not that, but against the *res* administered in the bankruptcy court. To get any standing, except as general creditors, they must identify the original assets, or trace them into other specific funds which came into the trustee's hands. It is not enough to show that they were converted by the bankrupt, or indeed that they may have generally enriched their estate." *In re Byrne,* 32 Fed. (2) 189, 190.

In *Wisdom v. Keen* (C. C. A. 5, 1934), 69 Fed. (2) 349 (cited with approved in *Adams v. Champion,* 79 L. Ed. Adv. 366, 369, the court said:

> "Equity if dealing with the bank alone might well consider that it had done what it should have done and might well hold it to the consequences. American National Bank v. Miller, 229 U. S. 517, 33 S. Ct. 883, 57 L. Ed. 1310. But in dealing with the distribution of the assets of an insolvent national bank and with the requirement of ratable dividends to all claimants a more stringent adherence to what was actually done is proper * * * as to every general creditor the bank has failed to do what it ought to have done and what it promised to do. The federal statute puts all such claimants on an equality." *Wisdom v. Keen,* 69 Fed. (2) 349, 350.

In *Maryland Casualty Co. v. Williams* (Ala., 1935), 159 So. 242, 244, the court, in denying a *cestui* recovery against an insolvent bank where the *res* had not been sufficiently traced, said:

"Equities against the bank, as such, and its stockholders, need not be considered. The assets of the bank have become a trust fund in which the equities of creditors are to be worked out." *Maryland Casualty Co. v. Williams,* 159 So. 242, 244.

There is only one situation in which the receiver has any burden of proof whatsoever. That arises under the following circumstances: In the majority of the Federal decisions the so-called low balance theory is approved, *i.e.,* that *after* the *cestui* has proved that his funds went into a commingled account and *after* the *cestui* has proved that the balance in said account contained *at all times* between the deposit and the receivership a balance greater than the amount of the trust fund deposit, and *after* the *cestui* has proved that there came into the hands of the receiver from such account a sum greater than the amount of the trust deposit, it will be presumed that the amount coming to the hands of the receiver from the account included the amount of the trust deposit. The courts, however, clearly state that this is a rebuttable presumption which will not stand against evidence to the contrary and that the receiver may adduce evidence to the effect that the trust moneys were actually earmarked and dissipated and thereby overcome the presumption that they remained in the low balance. See *Board of Commissioners v. Strawn,* 157 Fed. 49.

Mr. David R. Faries, in his Brief *Amicus Curiae,* in this proceeding, cites the language from five cases to the

effect that the burden of proof in tracing trust funds is on the receiver:

> *Meyers v. Baylor University* (Texas Civil Appeals), 6 S. W. (2) 393;
>
> *Grand Forks County v. Baird,* 54 N. Dak. 315, 209 N. W. 782;
>
> *Farmers' Bank v. Bailey,* 221 Ky. 55, 297 S. W. 938;
>
> *Hawaiian Pineapple Co. v. Browne,* 69 Mont. 140, 220 Pac. 1114;
>
> *Israel v. Woodruff* (C. C. A. 2, 1924), 299 Fed. 454, 457.

The first of these five cases, *Meyers v. Baylor University, supra,* was not even an insolvency case, but was merely against the tortfeasor trustee. Under such circumstances the courts feel no restrain in penalizing the trustee with as many presumptions and inferences as they can imagine.

The last of these five cases, *Israel v. Woodruff, supra,* was a case where the trustee had paid the *cestui* in full before his bankruptcy, and the trustee's receiver was endeavoring to recover the payment as an improper preference. Under the facts of the case there was practically an appropriation to the trust and the court said that to recover the funds the receiver had the burden of proving that they were not trust funds. Obviously a decision on such facts is not relevant to the Universal claim.

Finally, the first four of the said five cases are minority state cases, enunciating the oft repudiated principle that if

a claimant introduces evidence as to the amount of his trust funds and then merely shows that the receiver took over at least that amount among the assets of the insolvent, it will thereupon be presumed that the trust funds were included in the amount taken over by the receiver, without any showing whatsoever as to what happened to the funds between the time the trust arose and the date of the receivership. These four cases represent a principle which has been expressly and conclusively repudiated countless times by both the federal courts and the Supreme Court of California, as appears from the authorities cited in Point II (a) immediately following.

It is respectfully submitted that under the authority of the decisions of the United States Supreme Court and other circuit courts of appeal, cited in the four parts of this first point, it is established that the primary purpose of an equity receivership is to divide *pro rata* among all claimants the insolvent estate which is not sufficient to pay all of them in full as they had a right to be paid; that the fact that some of the claims arise out of fraud does not entitle such claimants to any preference, consideration, or "equity" over other claimants; that the federal courts will jealously guard equality of distribution as the highest equity, will only permit such equity to be disturbed by a clear proof that certain of the property in the custody of the court does not belong in the receivership estate at all, and will resolve all doubts and possibilities in favor of the receiver; and finally that such matters as sympathies and hardships must not be substituted for evidence, because the receiver and the creditor are not the *tortfeasor* who gave rise to such hardships and sympathies.

II.

It Is Respectfully Submitted That It Is Established by the Decisions Requiring the Cestui to Prove the "Low Balance" (Part (a) Below), by Reason and Banking Practice (Part (b) Below), and by the Unanimous Authority of Five Decisions Passing Directly on the Point, Two of Them Affirmed by the United States Supreme Court (Part (c) Below). That When a Claimant in Receivership Is Seeking to Trace Trust Funds Through a Commingled Account, Merely Showing the Overnight Balances of Such Account Is Not Prima Facie or Any Evidence of the "Low Balance" of Such Account. The Claimant Has the Absolute Burden of Proving the Actual "Low Balance" at All Times in the Account, and That Burden Never Shifts to the Receiver, for to Shift It Would Be to Grant an Improper Preference Under the Guise of Tracing Trust Funds.

(a) When the Low Balance Theory of Tracing Is Applied to an Account in Which Trust Funds and Other Funds Are Commingled, the Burden Is on the Cestui to Prove the Actual Low Balance Continuing in the Account at All Times Between the Time the Trust Funds Were Commingled in the Account and the Time to Which the Cestui Is Seeking to Trace Such Funds.

Blumenfeld v. Union Nat. Bank (C. C. A. 10, 1930), 38 Fed. (2) 455;

Kershaw v. Jenkins (C. C. A. 10, 1934), 71 Fed. (2) 647, 649;

Borman et al. v. Sullivan (C. C. A. 7, 1935), 77 Fed. (2) 342, 344;

In re Bogena & Williams (C. C. A. 7, 1935), 76 Fed. (2) 950, 953-4;

In re Mulligan (D. C. Mass. 1902), 116 Fed. 715;

Orcutt v. Gould (1897), 117 Cal. 315 (1897).

In *Blumenfeld v. Union Nat. Bank* (C. C. A. 10, 1930), 38 Fed. (2) 455, 456, the court said:

"In the instant case there is a dearth of evidence to show what amount of money remained in the Beloit bank through the period dating from the time it acquired the trust fund on July 28, 1922, to the date the receiver took charge on November 5, 1923. In the meantime, all its moneys, together with the trust fund, may have been disbursed. *The authorities cited establish that it is insufficient to trace the fund into the bank and to show that its cash or equivalent on its failure exceeded appellant's claim. If a trust fund is wholly depleted at any time, it cannot be treated as reappearing in subsequent accumulations, and a claimant of a trust fund has the burden of identifying it. Schuyler v. Littlefield,* 232 U. S. 707, 34 S. Ct. 466, 58 L. Ed. 806; *In re Brown* (C. C. A. 193 Fed. 24).

The appellant wholly failed to meet this burden of proof, and, the fund standing unidentified, he was not entitled to recover it preferentially from the receiver." (Italics ours.) *Blumenfeld v. Union Nat. Bank,* 38 Fed. (2) 455, 456-7.

In *Kershaw v. Jenkins* (C. C. A. 10, 1934), 71 Fed. (2) 647, 649, the court said:

"One seeking to impress a trust upon the assets of an insolvent national bank in the hands of a receiver must establish a fiduciary relationship between him-

> self and the bank in connection with the transaction giving rise to the claim, and he must trace the trust fund or property in its original or converted form into specific or identifiable property in the possession of the receiver. The trust *res* may be traced for that purpose *by proof clearly showing* that the assets of the bank were augumented through the transaction, *and, further, that the augmented fund was not depleted* intermediate the transaction and insolvency of the bank to a sum less than the amount of the claim. *Proof that the augmented fund was not so depleted is required* because a trust does not survive depletion and attach itself to subsequent accumulations. The equity of such a claim depends upon the effect the money or property of the *cestui que trust* had in swelling the assets *in the hands of the receiver.* * * * But, *if the proof fails to establish these essential elements,* full payment of the claim from money in the hands of the *receiver* for ratable distribution among *creditors* would be inequitable." (Italics ours.) *Kershaw v. Jenkins,* 71 Fed. (2) 647, 649.

In *Borman et al. v. Sullivan* (C. C. A. 7, 1935), 77 Fed. (2) 342, claimant requested her bank to buy certain bonds and gave it a check on the same bank for the purchase price on June 18, 1932. On June 20th the account of claimant was charged with the check and on June 21st a cashier's check was sent to the seller of the bonds by the bank, whereupon the bank picked up the bonds. On June 22, 1932, the bank closed and a receiver was appointed. The cashier's check was not honored and the seller of the bonds was permitted restitution thereof by the receiver. It was stipulated that the receiver took

over more in cash than the amount claimed as a trust fund by claimant. The court denied a tracing, saying:

> "Conceding without admitting that the bank's assets were augmented by the transaction, and that there was a trust created, yet we think appellants' contention must fail because no part of the so-called trust fund was traced into the hands of the receiver. The mingled funds were not ear-marked, and if the tracing of those funds into the receiver's hands is to be established it must be by virtue of the fact that at all times since the bank received the money in trust, it had enough currency on hand to equal the amount of the trust fund which it is claimed the receiver received. Appellants' check was delivered to the bank on June 18, 1932. It was not charged to appellants' account in the bank until June 20, 1932, and the bank was not closed until June 22, 1932. The stipulation is that when the bank was closed it had in its possession more than $2,065.98 in currency, which was paid to the receiver. The record does not disclose the status of the bank's currency account at any time between the time at which it is claimed the bank received the money in trust and the time it closed. The court can not indulge in the presumption that during that time the currency account remained sufficient to cover the claim or any part of it. *However short the intervening time, it was possible that the currency account was depleted and replenished,* and if it were once depleted there could be no tracing under the theory we are now discussing. St. Louis & S. F. R. R. v. Spiller, 274 U. S. 304, 47 S. Ct. 635, 71 L. Ed. 1060." (Italics ours.) *Borman et al. v. Sullivan,* 77 Fed. (2) 342, 344.

(b) From the Standpoint of Banking Practice and Reason, the Overnight Balances of a Bank Account Are Neither Prima Facie Evidence, Nor in Fact, Any Evidence at All That the Balance in the Account Did Not Fall Below the Closing Balance at Some Time During the Preceding Day, Especially Where the Amount of Checks and Deposits Entering Into the Account Each Day Is in Evidence.

There were three schedules introduced before the Master with respect to the bank account in which the Richfield funds were deposited: (1) the closing overnight balances shown on the bank's record for each day, (2) the intermediate balances entered on the bank's books during the course of each day, and (3) the total amount of checks and the total amount of deposits shown on the bank's books with respect to said account for each day.

The first of these was prepared by the Receiver and claimant and introduced by the claimant; the second of these was, at the request of the claimant, prepared and presented by the Receiver; and the third was prepared and presented by the Receiver in order that the Master, the courts and all the parties could have the advantage of all of the facts available. It was and is the opinion of the Receiver that the claimant had proved nothing without the introduction of this third schedule, even if successful on all of its legal contentions, and it has constantly been the policy of the Receiver, as an officer of the court, to make available at the hearings on claims all evidence within his power to produce, not only that against but that in favor of a claimant.

As to the so-called intermediate daily balances, the officers of the bank, the Special Master, the trial court,

this Honorable Court and every party to the action, including Universal and the Receiver, have repudiated these intermediate figures as not having any probative value in showing the low balance of the account, so we need not discuss these further.

As to the overnight balances taken alone, these have no more probative effect on the low balances in the account than the intermediate balances. The overnight balances do show the balances in the account for that *part* of the time *outside of business hours* when the account is *inactive,* but they show nothing whatsoever as to the low balance in the account *during business hours* when the account is *active.* It is respectfully submitted that this Honorable Court is in error when it states that the overnight balances only are accepted and used by both the bank and the customer in ordinary business transactions. True, these are the only balances of which the bank maintains a permanent record *after the day's business is concluded.* But from hour to hour and minute to minute throughout the day the bank recognizes changes in the account and, for example, would only certify checks against the true balance of the account at the minute when the check is presented for certification, regardless of what the opening or closing balance for the day might be. The court really affirms this practice when it says of the checks and deposits, "They react upon one another in rapid succession," or, in other words, that the balance in the account moves up and down rapidly throughout the business day.

It is submitted that the following is the true explanation of the bank's practice. The bank by accepting deposits from Richfield becomes the debtor of Richfield to

the extent of the deposits on an open book account. The fact that Richfield may have been trustee for Universal does not change the relationship between Richfield and the bank from that of a debtor and creditor relationship. The United States Supreme Court has so held even in the case of the trust funds deposited with the bank and known by the bank to be trust funds, saying, in *National Bank v. Insurance Company* (1881), 104 U. S. 54, 63, 64, 66:

> "A bank account, it is true, even when it is a trust fund, and designated as such by being kept in the name of the depositor *as trustee,* differs from other trust funds which are permanently invested in the name of the trustees for the sake of being held as such; for a bank account is made to be checked against, and represents a series of current transactions."
>
> "But although the relation between the bank and its depositor is that merely of *debtor and creditor*. and the balance due on the account is only a debt, yet the question is always open, To whom in equity does it beneficially belong?"
>
> *National Bank v. Insurance Company,* 104 U. S. 54, 63, 64, 66.

The bank held no cash of Richfield or of Universal, but was merely indebted to Richfield on an open book account, and Universal claimed an interest in that account. When the bank cashed, or accepted from the clearing house, a check drawn by Richfield, the bank, to that extent, discharged its indebtedness to Richfield and thereby reduced the account, whether or not the checks had yet been posted by the machines on the ledgers. The account was merely a chose in action which at any moment of time had no

existence other than in the then net balance of the debits and credits. Could it be contended for a minute that if the ledgers showed a balance of $100,000.00 on Richfield's account at 10:30 A. M. on January 15, 1931, the time of the inception of Richfield's receivership, and the bank had that morning cashed at its counters checks drawn on it by Richfield for $50,000.00, none of which checks had been posted, that the account between Richfield and the bank was still $100,000.00?

It was testified by the chief clerk of the bank that if a check was presented for payment or certification at any time during the day, the teller would look not only to the posted balance but also to the unposted items to ascertain the balance in the account. Thus, at any given moment of time the bank could ascertain the accurate balance of the account, although years later those conditions cannot be reconstructed. In order to assist the claimant should the Master determine all other issues in its favor, the Receiver put in evidence the only relevant evidence existing at the time as to the amount below which the balance in the account did not go, a schedule of the total of checks and the total of deposits entering into the account each day. Beyond this the means of ascertainment fail and as said in innumerable cases "when the means of ascertainment fail, the trust wholly fails, and the party can only prove as a general creditor."

> *Burnham v. Barth* (Wis., 1895), 62 N. W. 96, 98;
> *Multnomah County v. Oregon Nat. Bank* (C. C. Ore., 1894), 61 Fed. 912, 914.

To have the overnight balances evidentiary of the low balances in the account, it would be necessary to assume (1) that the *first* transaction *every* day was a deposit (for if it were a check the account would immediately and inevitably fall below the previous overnight balance); (2) that *throughout the day* deposits were made prior to the presentment of a corresponding amount of checks (for if the checks presented up to any given time during the day exceeded in amount the deposits made to that time, the account would necessarily fall below the last previous overnight balance); and (3) that the *last* transaction *every* day was a check (for if it was a deposit it would immediately be apparent that the account had been below the closing balance for the day). It is respectfully submitted that any such series of assumptions is wholly unsupported by evidence, reason or authority. Even the probabilities of the case overwhelmingly militate against any such assumptions. It is a well known fact of banking practice that the first batch of checks presented from the clearing house are presented in the morning *before* the bank opens its doors to depositors for the transaction of business and the making of deposits. This Honorable Court is well aware of this banking practice for it refers in its opinion to checks from the clearing house being presented at 8:15 A.M. Consequently, in an account as active as Richfield's, it would be practically impossible for the first transaction in the account each day, or for that matter any day, to be a deposit. Conversely, it is almost a certainty that the initial transaction in the account each day was a check necessarily drawing down the account

from the last previous overnight balance. Again, it is a frequent business practice to deposit the receipts for the day towards the closing of the banking day.

This account was the principal Richfield account covering many hundreds and even thousands of transactions a day. The members of this Court will know of their own experience that on the days when opening and closing balances in an account are highest the balance of the account in the middle of the day may be lowest. In an individual's account, if the only evidence given was the balance on January 1, 1930, and the balance on January 1, 1931, no one would contend that these balances indicated that the account never fell below the opening balance even though checks and deposits in amounts many times such balances went through the account during the year and there was no evidence of the order of such checks and deposits. The main bank account of Richfield which had over $84,000,000.00 of deposits made in it and over $84,000,000.00 of checks cashed against it during the period in which Universal seeks to trace its funds would probably have more transactions on a single day than the individual's account had during a whole year. The overnight balances of such an account could not possibly be any better evidence of the low balance in the account than the end of the year balances in the individual's account.

Coming now to the method used by the Special Master and the trial court in determining the amount which Universal had traced into the commingled account at the time

each investment was made therefrom, let us first hasten to say that there never has been a contention that the method used by the Master and the trial court established the actual low "balance" of the account. The method used does show, and it is respectfully submitted is the only evidence showing, the amount below which such low balance did not go.

At the hearing before the Special Master, a typical statement rendered to Richfield by the bank for November 22, 1929, showing an opening balance, numerous checks and deposits, several intermediate "balances" and a closing balance, was handed to witness McConnell, chief clerk of the bank, and the following questions were propounded and answers given:

> "Q. I have here a statement rendered to Richfield Oil Company by the Security Bank. The ones I am calling your attention to are the entries for November 22, 1929. If you were asked what was the maximum amount which that statement evidences remained in the account during the whole day, how would you ascertain that? A. The maximum amount—
>
> Q. Which remained in the bank account the whole day. A. The only way I could do that is by checking this balance ending November 21st, adding all these debits to the account, checks which have been charged, and subtracting it from them, and ignoring the credits entirely, is the only way I could give you an answer to that.
>
> Q. Is that any evidence that the account might not have fallen below that amount which you mentioned, to-wit; the opening balance, less all the checks? A. It couldn't fall below that balance.

Q. Is there any evidence that it remained above that? A. No, there is no evidence whatsoever.

Q. By Mr. Weil: On your assumption, you would have to assume that you started in with the balance of the day before, and that all the checks came in before there were any deposits, and that is what you did—you would just assume there were no deposits, and you would deduct that from the opening balance of the day? In other words, you would play safe? A. That is it exactly. I would do that instead of assuming that some of the deposits came in before the checks did."

It is respectfully submitted that if claimant had merely shown the overnight balances he would have adduced no evidence of low balance whatsoever. To the extent of the opening balance less all checks presented during the succeeding day, or conversely stated, the amount of the closing balance less all deposits made during the preceding day, the claimant could establish that the low balance, whatever it was in fact, was not below the figure thus arrived at. No other evidence introduced even indicated, let alone proved, that the low balance in the account was a greater amount. This method is not the use of a method of false accounting which takes into consideration checks and ignores equally important deposits. Rather, it is based on the legal and equitable rule that since the order of the checks and deposits is material to claimant's tracing, he must establish that order by proof or be limited to the amount which the evidence proved remained in the account. The deposits are not ignored. Rather, in the absence of proof as to the order of checks and deposits during any one day, the court is not warranted in assuming that any deposit was made before the presentation of the checks.

(c) It Is Respectfully and Earnestly Submitted That Not Only Does Banking Practice, Reason and Common Sense Require That the Overnight Balances Be Not Taken to Fix the Low Balances in the Account When the Amount of Checks and Deposits Each Day Are Known and in Evidence, But That Unanimous Weight of Authority Requires That in Tracing Trust Funds Against an Insolvent Estate Overnight Balances of a Bank Account Be Not Accepted as Prima Facie or Any Evidence of the Low Balance of the Account During the Active Daytime Periods Intervening.

Marshburn v. Williams (D. C., E. D., N. C., 1926), 15 Fed. (2) 589, 590. (Opinion by Circuit Judge Parker of the Circuit Court of Appeals, 4th Circuit);

Nixon State Bank v. First State Bank of Bridgeport (Ala. 1912. Rehearing denied 1913), 60 So. 868, 869-870;

Ex Parte First Nat. Bank of Princeton In re A. O. Brown & Co. (D. C., S. D., N. Y., 1911), 189 Fed. 432, 437-439; affirmed under name *In re Brown* (C. C. A. 2, 1912), 193 Fed. 24; affirmed under name *First Nat. Bk. of Princeton v. Littlefield* (1912), 226 U. S. 110;

Ex Parte Schuyler, Chadwick & Burnham In re A. O. Brown & Co. (D. C., S. D., N. Y., 1911), 189 Fed. 432, 433-435; reversed under name *In re A. O. Brown & Co.* (C. C. A. 2, 1912), 193 Fed. 30; reversal by C. C. A. affirmed under name *Schuyler v. Littlefield* (1914), 232 U. S. 707, 58 L. Ed. 806;

Connolly v. Lang (C. C. A. 7, 1933), 68 Fed. (2) 199, 201-202.

See:

Borman et al. v. Sullivan (C. C. A. 7, 1935), 77 Fed. (2) 342, 344.

It is submitted that the decision in this case is at variance with and diametrically opposed to the above cited decisions of the United States Supreme Court and the decisions in the Second, Fourth and Seventh Circuits.

In *Marshburn v. Williams* (D. C., E. D., N. C. 1926), 15 Fed. (2) 589, 590 (opinion by Circuit Judge Parker), a claimant sought to recover the proceeds of certain bonds amounting to $3,122.24 which it claimed were converted by the insolvent bank and that a trust was thereby raised. The proceeds were shown to have been deposited in an account of the insolvent with the American National Bank on December 15, 1922. On December 18, 1922, the insolvent drew checks on said account for $2,500.00 and $500.00 and deposited the same respectively to its account with the District National Bank of Washington and to its account with the Coal & Iron National Bank of New York. Shortly afterwards a receiver was appointed for the insolvent and the receiver took over balances of the insolvent from both the District National Bank and the Coal & Iron National Bank. Claimant asserted that it could trace its proceeds deposited in the account on December 15, 1922, into the deposits made from that account in the other two banks on December 18, 1922. Evidence of the overnight balances, the total amount of the checks and the total amount of the deposits on the days in question was presented to the court as follows:

	Opening Bal.	Checks	Deposits
Dec. 15	4608.38	27,000.00	24,275.74
Dec. 16	1884.32	16,946.80	23,241.31
Dec. 17	Holiday		
Dec. 18	8178.85	39,101.75	15,777.43

On this evidence the court held that because of the amount and number of checks against the account with the American National Bank between December 15 and December 18, claimant had not shown that any of the trust funds remained in the account on the latter date and that therefore none of the trust funds were included in the checks on this account deposited with the District National Bank and the Coal & Iron National Bank, saying:

> "Complainant claims a balance of $887.94 in the District National Bank of Washington, because on December 18th the Commercial drew a check on its account in the American for $2500 in favor of that bank. Complainant likewise claims $500 of a balance of $845.05 in the Coal & Iron National Bank of New York, because on December 18th $500 was transferred by the Commercial to the Coal & Iron National from the American. But an examination of the account with the American, which has been filed with the record, shows that these deposits in the District National of Washington and the Coal & Iron National of New York cannot be said in any sense to be the proceeds of the bonds in controversy. The Commercial had an Active Running Account With the American, which showed each day debits and credits of large amounts. On December 15th, the day when the bonds were debited against the American, the account was debited with another item of $21,153.50. The balance from the preceding day was $4,608.38. On the 15th the Commercial drew checks against the account for $7,000, $5,000, and $15,000, respectively

leaving a balance, as stated above, of only $1,884.32. On the 16th, the account of the American was debited with items of $22,091.28 and $1,150.03, against which there were withdrawals of $16,520.29, $210.67, $114.34, and $101.50, leaving a balance of $8,178.85. On the next business day, the 18th, the account was debited with items of $2.10, $2,254.78, $378.44, $1,558.80, and $11,583.31, against which there were withdrawals of $10,000, $10,000, $15,000, $1,000, and $101.75, in addition to the $2,500 to the District National and the $500 to the Coal & Iron National, leaving an overdraft, as above stated, of $15,145.47.

"This being the state of the account of the Commercial with the American between the time of the forwarding of the bonds and the sending of the checks to the District National and the Coal & Iron National, it is perfectly clear to my mind that complainant has not traced into the moneys sent to the District National and the Coal & Iron National the proceeds of the bonds in controversy or any part thereof, but that, on the contrary, it is shown that the proceeds of the bonds were inextricably intermingled with other assets of the bank."

Marshburn v. Williams, 15 Fed. (2) 589, 590.

Similar facts to those in the foregoing case are presented innumerable times in the Richfield account. For instance, the facts for the period between December 23, 1929, and December 27, 1929, are as follows:

	Opening Bal.	Checks	Deposits
Dec. 23	949,358.12	848,223.61	417,606.58
Dec. 24	518,741.09	594,773.93	744,367.08
Dec. 25	Holiday		
Dec. 26	668,334.24	339,778.49	193,252.09
Dec. 27	521,807.84	516,584.02	319,830.72

It is respectfully submitted that this Court should have held that there was no evidence that the account was not overdrawn on December 24, 1929, and that this Court erred in looking at merely the overnight balances and finding that there were trust funds in the opening balance December 23rd which remained in the account and entered into investments made out of the account after December 27, 1929.

In *Nixon State Bank v. First State Bank of Bridgeport* (Ala. 1912—rehearing denied 1913), 60 So. 868, 869-870, the Nixon State Bank (Texas) sent a note for $820 to the First State Bank (Ala.) for collection. The First State Bank collected by check of Wrenne & Co. and sent the latter check to the First National Bank (Nashville, Tenn.) for collection. The check was collected and the First National Bank placed in to the credit of the First State Bank in the account between them on May 14, 1910. On May 28, 1910, the First State Bank went into the hands of a receiver and the First National Bank turned over to said receiver the balance of the account amounting to $1,193.61. The Nixon State Bank claimed $820 as a trust fund but this was denied, the court saying:

> "From May 13th to May 21st, both inclusive, the First State Bank remitted to the First National Bank of Nashville collections aggregating, daily, $1,012.73, $323.16, $763.95, $363.89, $163.75, $1,066.77, $259.-37, and $114.60. The daily *balances* with the First National Bank to the credit of the First State Bank, from May 14th to May 28th, both inclusive, varied between $375.40, the lowest, and $1,653.64, the highest; the balance on the last day being the said sum paid over by the First National to the receiver of the First State Bank. * * *

"The state of the account, and the varied, daily changes in its balances, between the insolvent bank and the First National Bank rendered it impossible that the proceeds, if such was the result, of the Talley note could be traced or identified with the precision necessary in order to impress it with a trust character, which equity, upon proper occasion, imposes to preserve, protect, and enforce the right of a principal whose property has been converted by the agent. It cannot be here held, as it was not in the decision mentioned, that the fund so received by the receiver was composed, in whole or in part, of the product of the payment of the Talley note. Indeed, the net daily balances between the insolvent bank and the First National Bank, subsequent to May 14, 1910, aggregate many thousands of dollars—a shifting, varying matter of daily credit and debit in the process of the daily adjusting of the account between them. The sum delivered to the receiver may as well have been the creation of credits sent, above debits made, to the First National by the insolvent bank on any day *after,* say, May 18th.

"The suggestion that the lowest balance with the First National Bank existing after May 14th, which was $375.00, on May 16th, should be taken as composed of a part of the Wrenne & Co. check, upon which the Talley note was surrendered, cannot be adopted otherwise than arbitrarily. The gist of the pertinent doctrine of the Florence Bank decision is that, where funds or property of the principal are commingled by the agent with his property or funds, equity cannot effect its just purpose to impress the fund or property with a trust character, for the benefit of the principal, unless the principal's funds or property can be distinguished—can be distinctly traced.

The considerations stated prevent the application of the doctrine, for that the funds, if so, of the petitioning bank cannot be distinguished."

Nixon State Bank v. First State Bank of Bridgeport, 60 So. 868, 869-870.

The opinion in *Ex Parte First Nat. Bank of Princeton In re A. O. Brown & Co.* (D. C., S. D., N. Y., 1911), 189 Fed. 432, 437-439, was written by Judge Hand, who had previously written the opinion *Primeau v. Granfield* (D. C., N. Y. 1911), 184 Fed. 480, relied upon by claimant. The claim of First National Bank of Princeton and several others *were treated as one,* since all sought to make their claims good through the account of the bankrupt in the Hanover Bank. Consequently, conflicting claims of different *cestuis* were eliminated. All of the trust funds of these parties had gone into the Hanover Bank before August 24th with one exception. The court said:

"On the morning of August 24th that account contained over *$130,000,* and they had a lien on *it,* for what money of theirs had gone into *it,* under Knatchbull v. Hallett, *supra.* On the morning of the 25th the account contained about $6,200, which was at once entirely withdrawn and the account reduced to nothing. * * * The claims here must therefore depend upon the transactions of the 24th. On that day over $3,700,000 was deposited in the account, and over $3,800,000 was withdrawn." (Italics ours.)

Ex Parte First Nat. Bank of Princeton In re A. O. Brown & Co., 189 Fed. 432, 437-439.

The various theories of claimants that they could claim securities bought with checks on said account on the 24th, and that they could claim collateral released by the payment of a designated secured loan of $200,000, which payment and release of collateral was made with a check on said account on the 24th, are reviewed by the court, which then says:

> "There is, however, no theory which does not involve the hypothesis that *up to the time of the supposed investment in the stocks in question the fund had remained continuously equal to the amount of the claims.* For example although the claimants were all entitled to a lien to the amount of their claims upon the account at the opening of business on the 24th, *yet if that account had been at any time that day reduced below that amount*, subsequent deposits would not restore to the claimants their rights. There is no presumption of an intent to restore, and in the case at bar it would be an obvious fiction. Now on the 24th the transactions were enormous. Only a part of the stock purchased was of the kind pledged upon these four loans. Indeed there were *drawn* over $400,000 of checks for other purposes before any check was drawn to pay for any stocks of the kind placed with the loans. It is true that the order of drawing the checks is in no sense the same as the order of presenting them, but the fact mentioned at least shows the *possibility. The claimants therefore failed to prove that at the time of the alleged investments any of their money remained in the account, and that is a necessary step in tracing their money into any particular part of the estate."* (Italics ours.)
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> *In re A. C. Brown & Co.,* 189 Fed. 432, 438.

It should be noticed that when considering the proof, the court points out only the amount of checks drawn, and makes no mention of the deposits, for there was no evidence of their order. The court goes on to say that *cestui* must prove the amount in the account *at all times* during the day, saying it will not be presumed that the opening balance remained.

> "Nor is there any presumption in the case that the fund always remained large enough to answer the trust moneys. The very first check *drawn* was greater than the opening balance and *it is the merest speculation to assume what were the deposits or what the amount in the bank's account all day long.* While equity will follow funds as long as they can be traced, it always requires affirmative proof by the beneficiary that his money went into some specific thing. Here, that proof would require *the claimants at least to show that at the time of each investment* which they claim their money was in the bank—I mean at least that much money. The same reasoning applies as to the payment of the $200,000 note. * * *
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> "I need not therefore consider whether, for the purpose of establishing a lien, the beneficiary may select any earlier withdrawal which went into an investment and which has been preserved. If the general mixed fund has been wholly dissipated, it has been held that he may do so (*Re* Oatway, 1903, 2 Ch. Div. 356), and that Knatchbull v. Hallett, *supra*, does not limit him to a line only where the result will be to prevent his following his money. That presupposes what has not been shown in this case; that is, that the supposed investment was in fact made from a mixed fund. *The claimants have throughout assumed that throughout the 24th the fund remained large*

enough to cover their claims, and it is upon that rock that, in my judgment, their theory is wrecked." (Italics ours.)

In re A. C. Brown & Co., 189 Fed. 432, 438, 439.

There is no equivocation in this holding by Judge Hand made later than and referring to his decision in *Primeau v. Granfield.* There is no room for distinguishing the case on the ground that the account was overdrawn on the 25th, for his decision is with respect to investments made on the 24th. There is no room for distinguishing the case on the ground that the investments were not clearly pointed out and traced, for at least with respect to loan paid off, the particular investment was pointed out, proven and the collateral entirely traceable. The court based its decision on the ground that there was no tracing of the trust funds *into the account* immediately prior to the making of the *investment.* He refused to accept the opening balance for the day as evidence of the amount remaining in the account during the day at least when there was evidence as to the amount of checks and deposits entered on the account during the day but no evidence as to their order.

In the *Richfield* case a similar instance is found on February 25, 1930. On that day the opening balance was $296,779.62. The amount of checks charged against the account was $425,191.72, the amount of deposits in the account $381,172.34 and the closing balance $252,-760.24. This Honorable Court, contrary to the finding of the special master, contrary to the finding of the trial court, and contrary to the authority of the above described case, held that trust funds remained in the account all day to the extent of $252,760.24.

The decision of Judge Hand on the Princeton Bank claim was affirmed by the Circuit Court of Appeals, Second Circuit, in *In re Brown*, 193 Fed. 24. The claim of the Princeton Bank arose from moneys paid to Brown & Company by the Princeton Bank with which to buy stock. Brown & Company bought the stock, but then sold it and retained the proceeds. The Circuit Court of Appeals for the Second Circuit had ruled earlier that the Princeton Bank could not rescind and trace the money it paid to Brown & Company, but that it was entitled to the proceeds of the converted stock and should be permitted an opportunity to trace these proceeds if it could. 175 Fed. 769. The Circuit Court of Appeals gives more detailed facts than the trial court. Certain of the claimants' moneys were deposited in the Bank of Commerce and the court finds these were dissipated. Next the court took up the separate question of deposits of money of the Princeton Bank in the account of the bankrupt in the Hanover Bank prior to the 25th. These deposits had been made from August 13th to August 24th, and the special master had found that "the opening and closing balances in the Hanover Bank on and after August 13th were largely in excess of these deposits." The Circuit Court of Appeals held that this finding was not sufficient to show a tracing of the Princeton Bank's money into the account on August 24th for two reasons—1st: these balances might as well represent the trust money of other claimants (none of whom had been able to trace and who were therefore relegated to the position of general creditors, just as in the case of Richfield), and 2nd: that in any event opening and closing balances are not evidence that the entire account was not dissipated. The court said of the master's finding on opening and closing balances:

"But the finding is not sufficient; there is no reason why it should be assumed that these balances were being reserved because they represented the trust money of the Princeton Bank, rather than because they represented trust money of Simpson, or Scrotton, or any of the other similarly situated enumerated above (aggregating $21,783.39)—or, indeed, any of the other claimants who from time to time have appeared in this proceeding seeking to trace and recover for property converted by the bankrupts.

"*Moreover,* it is not enough to show that there were morning and afternoon balances for several successive days large enough to cover the amount of money which was improperly converted. It might very well be that on any one day checks were presented which exhausted the morning balance and its accretions, in which event these moneys would have been dissipated. We are not prepared to assent to the proposition that subsequent deposits are to be taken as having been made to make good claimant's money thus drawn and spent. Board of Commissioners v. Strawn, 157 Fed. 51, 84 C. C. A. 553, 15 L. R. A. (N. S.) 1100. Our own conclusion would be that the $1,757.50 of the proceeds of claimant's stock, which went into the Hanover Bank on August 13th, has not been shown to be any part of the balance which was turned over by that bank to the trustee * * *"

In re Brown, 193 Fed. 24, 26.

The last mentioned decision of the Circuit Court of Appeals was not involved with anything that occurred in the account on August 25th. The court felt that possibly the special master and the trial court had some additional evidence as to what happened to the balance in the ac-

count during each day, so he then went on to consider transactions on the 25th. With respect to the deposit of the Princeton Bank on August 13th the court said:

> "Nevertheless the master and the District Judge seem to have reached the conclusion that it remained in the account on August 24th. Since both of them had the same understanding of the law as that above expressed, viz., that the first check drawn on any given day might sweep away the balance carried over, *and that it would be the merest speculation* to assume that subsequent deposits restored the original situation, it is possible that they had some evidence, which is not in this record, as to the *continuous* condition of the daily balances prior to December 24th. Moreover, there is the deposit of claimant's proceeds to the extent of $280 on the 24th, which makes it necessary to consider the transactions of that day and the next." (Italics ours.)
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> *In re Brown,* 193 Fed. 24, 26-27.

The court then found that sometime on the 25th the Hanover Bank account was drawn down to nothing, so that any tracing of funds deposited on August 13th or August 24th into the balance of the account remaining on the failure of Brown & Company on August 25th was impossible.

This opinion of the Circuit Court of Appeals was affirmed under the name *First National Bank of Princeton v. Littlefield* (1912), 226 U. S. 110, 57 L. Ed. 145, the court saying:

> "The report of the master was confirmed by the district court (189 Fed. 432, 442), and the action of that court was in all respects affirmed by the circuit court of appeals (113 C. C. A. 348, 193 Fed. 24.)
> * * *

"All the contentions relied upon in various forms simply assert that the master and the two courts erred in their appreciation of the facts. *But the burden of proof was upon the claimant to establish its ownership of the fund*—a burden which it cannot in reason be said was sustained in view of the concurrent adverse action of the master and the courts below."

First National Bank of Princeton v. Littlefield, 226 U. S. 110, 57 L. Ed. 145.

Ex parte Schuyler, Chadwick & Burnham In re A. O. Brown & Co. (D. C., S. D., N. Y. 1911), 189 Fed. 432, 433-435, is one of the decisions relied upon by claimant. The opinion is written by Judge Hand, who it will be recalled had previously written the opinion in *Primeau v. Granfield* (D. C., N. Y. 1911), 184 Fed. 480. The Brown & Company bankruptcy gave rise to a number of claims, among them that of Schuyler, Chadwick and Burnham. The facts of the Schuyler claim were that the bankrupt had converted certain stock of Schuyler by selling it in a single batch along with other stock to Miller. This was done on August 24, 1908, and Miller gave the bankrupt two checks for the purchase price on that date, one for $266,600.00 issued first, and one for $23,000.00 issued later the same day. Judge Hand said that treating the obligation of Miller to pay for the stock as if it were a bank account, in the absence of other evidence, when the first check was drawn the claimant could say his money remained in the obligation of Miller; then when the second check was drawn for the balance of the obligation, the claimant's money was necessarily in it. In passing, it should be called to the attention of the Court that obviously such a holding does not involve any appli-

cation of the doctrine of *In re Oatway* as contended by Mr. Faries. It was conceded by the trustee in bankruptcy that the $23,000.00 check had been issued to pay a loan which released collateral and that such released collateral or the proceeds thereof had come into the hands of the trustee. Upon these facts Judge Hand held that the proceeds of claimant's stock had been traced to property in the trustee's hands.

Judge Hand's decision in the District Court was reversed by the Circuit Court of Appeals, Second Circuit, in the case of *In re A. O. Brown & Co.*, 193 Fed. 30. The Circuit Court of Appeals stated that the larger check was deposited in the Hanover Bank in Brown & Company's account on the 24th of August and the smaller on the 25th of August. At noon on the 25th of August, Brown & Company made an assignment for creditors and the Hanover Bank turned over the balance of the account to the assignee, who in due course turned it over to the trustee in bankruptcy. The Circuit Court of Appeals said that it was not satisfied that the claimant's fund had been traced to the second check as distinguished from the first check, but that it made no difference since in its opinion the proceeds of neither check had been traced to the hands of the trustee in bankruptcy. It was established that some time on the morning of August 25th, probably about 11:00 o'clock A. M., the account with the Hanover Bank was drawn down to nothing by the certification of a check which exhausted the entire balance then in the account. There was a balance in the account, however, to turn over to the assignee for creditors at noon on the 25th. The Court said that if the claimant's money was in the earlier check deposited on August 24th it surely was in the balance remaining in the account at noon on

August 25th, since the account had been exhausted at one time on the morning of August 25th. The court further said that if claimant's funds were in the smaller check deposited on August 25th, claimant had failed to show that the amount claimed by him remained in the bank to the time it failed, because he had failed to show the relative order of the check which drew down the account and the deposit of $23,000.00 in which he claims his funds were included. The court specifically found that the order of checks and deposits on the books of the bank could not be used, since the officers testified (as in the Universal case) that this order on the books was not necessarily the order of the actual transaction. In reversing the lower court, the Circuit Court of Appeals said:

> "It is the theory of the claimant that this $23,000 was not deposited until after the large check to A. H. Combs & Co. ($146,600) had been certified; it being contended that for that reason the proceeds of claimant's stock, which it is claimed were included in the $23,000 check, were not dissipated by the certification. To maintain this theory it is necessary for the claimant to show by competent proof which event occurred first, the certification or the deposit. * * *
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> "In order to establish the relative priorities of the certification and of the deposit of the $23,000 check, it is necessary to show the time when both transactions took place. But as to the deposit there is no testimony whatever. In view of the circumstance that the deposit slip was prepared in the afternoon of the 24th, and that the condition of Brown & Co. was such as to call for the prompt deposit of everything they could control, it might fairly be inferred that the $23,000 would be deposited on the 25th, as soon

as the bank opened; but it is not necessary to draw inferences. *It is for the claimant to show when* the $23,000 was deposited if that time is essential to his argument. *He cannot trace his money by a mere succession of presumptions.* Some of the modern cases have gone very far—possibly in some instances too far—in helping out a claimant by presumptions not always reasonable; but in this circuit we have always required some substantive proof as a basis for holding that the owner of trust funds converted by a bankrupt has a lien on some particular part of the *bankrupt's property.* Carse, the vice-president, testified that the $66,600 check was the first deposit on the 25th, to his recollection—a very uncertain recollection, as we have seen—but no one testified and no writing of any sort was introduced to show when the $23,000 was deposited. We cannot therefore find that it was deposited after the certification, and, since the evidence establishes quite conclusively that the $146,600 check was not certified until 11 a. m. or later, there is nothing to show that the $23,000 check and all the others (except perhaps the $17,300) were not absorbed by the certification. If the claimant's $9,600 was included in the $23,000 check, it was then dissipated and can be traced no farther." (Italics ours.)

> *In re A. O. Brown & Co.,* 193 Fed. 30, 31, 32-33.

The decision of the Circuit Court of Appeals for the Second Circuit, which reversed the trial court. was affirmed by the United States Supreme Court in *Schuyler v. Littlefield* (1914), 232 U. S. 707. With respect to the moneys coming to the trustee's hands from the Hanover Bank, the Supreme Court agreed that the claim-

ant had not traced any trust funds to the balance on hand at noon on August 25th. It stated that if the trust fund was included in the check deposited on the 24th then it was dissipated, at least down to the closing balance on August 24th, and the remainder dissipated the next day. The statement of the court that it was dissipated down to the balance at the close of business on the 24th cannot by the widest stretch of the imagination be construed to be a holding by the court that the balance at the close of business on August 24th constituted trust funds. It merely shows that regardless of any other evidence the trust would have been entirely dissipated by reason of the closing balance on August 24th and the depletion of the account the next morning. Treating the trust fund as being included in the check deposited on the 25th, upon the lack of evidence as to the order of the checks and deposits on that day, the court affirmed the assumption of the trial court that the deposit of $23,000 was made before the certification of the check which depleted the account.

The holding of this Honorable Court with respect to the Universal claim that, when the order of checks and deposits is not shown, Universal's money will be held to remain in the closing balance for the day is, we submit, wholly irreconcilable with the decision of the Circuit Court of Appeals, Second Circuit, expressly approved by the United States Supreme Court, to the effect that in the absence of a showing as to the order of checks and deposits even for one or two hours during the day, it must be found that the checks presented drew down the account and the trust funds cannot be held to continue to exist in the account to the full extent of the closing balance for the day.

A similar instance in the Richfield account is found on February 25, 1930. The facts as to that day were:

Opening Bal.	Checks.	Deposits.	Closing Bal.
296,779.62	425,191.72	281,172.34	252,760.24

Of the deposits, $100,000 came from Universal. Contrary to the above described case affirmed by the United States Supreme Court, this court merely assumed that as the balance at the end of the day was over $100,000 the deposit of Universal funds in that amount were shown to have remained in the account. It is respectfully submitted that since the checks for the day exceeded the opening balance by more than $100,000, in the absence of any evidence as to when the deposit was made with relation to the checks and other deposits, the court should have held there had been no tracing of the trust deposit into the closing balance.

In *Connolly v. Lang* (C. C. A. 7, 1933), 68 Fed. (2) 199, the facts were that on June 22, 1932, a savings depositor in an outlying Chicago bank made a request to withdraw her deposit totalling $9642.83 at that time. Her account sheet was pulled from the books and her passbook marked to indicate the withdrawal. Upon her then explaining that she wanted to take the money to a downtown bank to buy a draft to go to Europe she was advised that the outlying bank could accommodate her. They gave her a draft on a New York bank for $8,500.00 and the balance of $1142.73 in cash. The bank wired $5000.00 to the N. Y. bank which, in addition to its funds already with the N. Y. bank, were intended to cover the draft. June 22, 1935, was the last day the bank was open and next morning a receiver took over its assets

including the account in the N. Y. bank, so that the draft issued to the former depositor was never honored.

The depositor claimed the full $8500.00 out of funds coming to the receiver. The court found that the funds of the bank at the closing thereof on June 22, 1935, and which were delivered to the receiver exceeded the amount claimed by the depositor.

The court said this was not sufficient to enable the depositor to succeed, saying:

> "While it is found that at the time the bank was closed it had on hand more than the amount of appellee's claim in cash, which appellant received, yet that does not necessarily mean that that sum included any part of appellee's money. The cash balance of the bank, if any, at the beginning of business on June 22, 1932, is not disclosed, *nor are the deposits and withdrawals shown for that day.* Those facts if shown would reveal what funds, if any, the bank had at the time of appellee's transaction. If, at that time, there were no funds in the bank except the amount she received in cash, and the amount wired to Central Hanover, then it is clear that there would have been no funds to which the alleged trust could attach except the money held by Central Hanover. *If the trust is once depleted, it can not be built up by subsequent deposits of other depositors.* Schuyler v. Littlefield, *supra;* Blumenfeld v. Union National Bank (C. C. A.), 38 F. (2d) 455; *In re B*rown (C. C. A.), 193 F. 24. We cannot say that the cash balance of the bank on the morning it failed to open was not received by the bank subsequent to appellee's transaction." (Italics ours.) *Connolly v. Lang,* 68 Fed. (2) 199, 201.

> "If this were a controversy only between appellee and the bank there might be good reason for permitting fiction to pervert the facts because all the equities would be with appellee. This action, however, is really between appellee and the general depositors, who without fault on their part have been placed in positions which no doubt are equally deplorable and *whose rights to have equity done are equally worthy of consideration.*" (Italics ours.) *Connolly v. Lang,* 68 Fed. (2) 199, 202.

Mr. David R. Faries, in his brief *amicus curiae,* cites one additional case which he contends is authority for the contention that the burden of proof is on the receiver. In *Smith v. Mottley* (C. C. A. 6, 1906), 150 Fed. 266, cited on page 160 of Mr. Faries' brief, Mr. Faries misstates the facts, and it is only by reason of his misstatement that he can find any solace in this case. Mr. Faries states that the only proof was that the bank "had wrongfully received the beneficiary's money some ten days prior to the general assignment for the benefit of creditors." The amount sought to be traced was $2,315.23 received by the trustee on April 11, 1905. The court specifically found "From the 11th day of April to the time of making its assignment, the bank had on hand at all times more than $7,000 in cash, and the assignee, who is now the trustee, received more than that sum." Consequently, the claimant had sustained the burden of showing the continuous condition of the account at every minute in the intervening period. All discussion about the burden of proof being on the trustee in bankruptcy has to do with the burden of proof to show that the trust funds did *not* in fact remain in the low balance *after* the *cestui* has established what that low bal-

ance is. As said in *In re Brown* (C. C. A. 2), 193 Fed. 24, 29, the general language of *Smith v. Mottley* is controlled by the later decision in the same court of *Board of Commissioners v. Strawm* (C. C. A. 2), 157 Fed. 49. The other cases cited by Mr. Faries are discussed and shown to be clearly irrelevant on other pages of this petition.

It is respectfully submitted that the *only* evidence of low balance of the account is that provided by combining the overnight balances with a consideration of the amount of checks and deposits made each day, the burden of proof being on the claimant to show which if any deposits preceded which if any checks. In the absence of any proof of the order of the checks and deposits, it should not be assumed that any deposit was made before the checks were presented, at the expense of the other creditors of the estate. Mr. Faries' illustration on page 22 of his brief *amicus curiae* is misleading and incorrect. He says that if the opening balance was $1,000.00 and a deposit for $200.00 was made and thereafter a check for $200.00 was cashed, the Master would assume that the low balance for the day was $800.00. He is entirely incorrect in his prediction of what the Master would find. *If* Universal had been able to show the order of checks and deposits, as assumed by Mr. Faries, the Master would have found that the low balance for the day was $1,000.00.

It is submitted that the very fact that the court rules that the burden of proof as to an essential element of tracing is on the Receiver shows conclusively that some fact in the tracing is missing and that Universal has not completed a tracing of its funds. To shift the burden

of proof to the receivership estate and the creditors, or to dispense with proof in any other manner, is merely granting an improper preference to Universal while attempting to disguise it under the name of tracing trust funds.

In *Jennings v. U. S. Fidelity & Guaranty Co.* (1935), 79 L. Ed. Adv. 355-360, a state statute attempted to provide a trust for a certain class of creditors without the necessity of tracing. The Supreme Court, in refusing to apply this statute to a receivership of a national bank, said:

> "A trust so created, to arise upon insolvency, is a preference under another name. As applied to a national bank, the preference is plainly inconsistent with the system of equal distribution established by the federal law."
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> *Jennings v. U. S. Fidelity & Guaranty Co.*, 79 L. Ed. Adv. 355, 360.

In *In re Mulligan* (D. C. Mass. 1902), 116 Fed. 715, 718, the court says that since a tracing is proper and a preference is improper, the court should not disguise a preference as a tracing by shifting the burden of proof, saying:

> "* * * to change the cestui's claim for priority into a mere shifting of the burden of proof finds no considerable support in the decided cases."
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> *In re Mulligan* (D. C. Mass. 1902), 116 Fed. 715, 718.

III.

The Supreme Court of the State of California Has Established as a Rule of Property for that State That as Against Creditors of a Trustee ex Maleficio the Cestui Has No Interest in a Bank Account of the Trustee in Which Funds of the Cestui and Trustee Have Been Commingled After Checks to the Amount of the Cestui's Funds in the Account Have Been Charged Against That Account. Under This Rule of Property and the Facts Established in This Case, Universal Had No Interest in the Richfield Bank Account at the Time the Several Investments, Which Are the Subject of This Proceeding, Were Made and Consequently Could Have No Interest in the Investments. As Both the Bank Account and All of the Properties Involved Are Properties in the State of California, and in Most Cases Are Interests in Real Property in the State of California, the Above California Rule of Property Should and Must Be Followed by the Federal Courts.

In his Brief *Amicus Curiae* in this proceeding, Mr. David R. Faries calls the Court's attention to a portion of the opinion in *Mitchell v. Dunn* (1930), 211 Cal. 129, claims that this establishes the law of California in favor of the contentions of Universal, and asserts that the California decision should be given great consideration. We deny that, under the facts of this case with the trustee insolvent, Universal can find any solace in the decisions of California. See *Mitchell v. Dunn, supra,* page 136. Rather, it is submitted, that under the facts established in this case, the established rules of property in California deny any interest in the properties in question to Univer-

sal, and such rules of property not only should be considered by, but are binding upon, the federal courts.

The California Supreme Court has rendered a long line of decisions on the tracing of trust funds. Long before the high court of England (*Knatchbull v. Hallett,* 1880, L. D. 13, Ch. Div. 696, 743) and the high court of the United States (*National Bank v. Insurance Co.,* 1881, 104 U. S. 54) relaxed the early rule that if trust moneys were commingled with the moneys of the trustee, they could no longer be traced, the California Supreme Court reached this same more liberal conclusion in the case of *Gunter v. Janes* (1858), 9 Cal. 643, 660-661. In that case a *cestui que trust* was permitted to recover his money from a commingled fund, there being no creditors of the trustee involved, the court saying:

> "We cannot perceive, upon considerations of principle or utility, why the mingling of trust with private moneys, by the voluntary act of the trustee, should destroy the trust fund, and change the remedy or right of the beneficiary. It is true, money has no earmarks; and, for that very reason, the mingling of trust with private funds can injure no one. The value being the same, and it being matter of the most perfect indifference whether parties get the same or other coin, so they get the sum to which each is entitled, there can result no injury to either. Common sense will not discuss the question of identity, when nothing useful can result from its determination."

In speaking of several English cases not permitting a trust in commingled funds, the court said:

> "But these cases are clearly distinguishable from the case before us. There the rights of creditors

were involved, while here the contest is solely between the *cestui que trust* and the administrator of the trustee."

Gunter v. Janes, 9 Cal. 643, 660-661.

After a full consideration of the decisions *in re Hallett's Estate, supra; National Bank v. Insurance Co., supra,* and other Federal and California cases, the California Supreme Court decided that in California, as against creditors of an insolvent trustee *ex malificio,* the *cestui* had no interest in a bank account of the trustee in which the *cestui's* money had been commingled with that of the trustee if the amount of checks charged against the account from the time of the deposit of the *cestui's* funds exceeded the amount of such funds.

People v. California Safe Deposit & Trust Co. (1917), 175 Cal. 756.

In the latter case the Trustee Company fraudulently induced claimant to buy its stock for $12,000.00. The Trust Company went into insolvency proceedings and the claimant sought to impress a trust upon funds coming into the Trust Company receiver's hands. The evidence shows that the Trust Company's cash never fell below $123,000 between the time claimant bought the stock and the time the Trust Company closed its doors. Meanwhile about $6,000,000.00 of deposits and withdrawals were made. The lower court said that the presumption that claimant's funds were still in the bank did not apply against creditors where the trustee was such by reason of his own fraud and held that claimant had failed to trace his funds into the balance taken over by the receiver. The Appellate Court affirmed the judgment against claimant, saying:

"Upon this appeal the appellant insists that he was entitled to payment in full, rather than as a general or common creditor. His position is that the bank became an involuntary trustee of the twelve thousand dollars which it had obtained from him by fraud (Civ. Code, sec. 2224), and that he had sufficiently traced this trust fund into the hands of the receiver to be entitled to payment in preference to general creditors. It is well settled that the beneficiary of a trust may follow and recover the trust fund if any property in the hands of the trustee or of those taking with notice can be identified either as the original property of the *cestui que trust,* or as the product of it. (Thompson's Appeal, 22 Pa. St. 16.) Where, however, the identity of the trust fund has been lost, the beneficiary is relegated to the position of a general creditor, and must share pro rata with other general creditors. (Lathrop v. Bampton, 31 Cal. 17, 89 Am. Dec. 141.)

"The appellant insists that upon these facts the court was bound to find that the twelve thousand dollars received from him, as aforesaid, remained intact in the hands of the bank during the entire period intervening between the purchase of the stock and the closing of the bank, and that such fund had been identified and traced into the hands of the receiver. The argument is that since it appears that the bank had on hand at all times a sum in excess of twelve thousand dollars, the amount claimed by the petitioner, it must be presumed that it retained this sum to meet his claim arising from the fraud perpetrated upon him. The argument is based upon the well-settled rule that if a trustee mingles his own funds with the trust fund, and thereafter draws from time to time from the commingled mass, 'it will be pre-

sumed that the moneys so drawn were from his own portion of the fund, rather than from the moneys held by him in trust.' (Elizalde v. Elizalde, 137 Cal. 634, 641 (66 Pac. 369, 70 Pac. 861); *In re Hallett's* Estate, L. R. 13 Ch. Div. 696; National Bank v. Insurance Co., 104 U. S. 54 (26 L. Ed. 693); Lewin on Trusts, 895.) Various expressions have been used in defining the nature of the rule. In some of the cases, as pointed out by the appellant, it has been said that equity will 'attribute' the withdrawals to the trustee's private account. In others, as in the Elizalde case above cited, it is said that the trustee will be 'presumed' to have drawn his own money. In one case (Crawford County Commrs. v. Strawn, 157 Fed. 49 (15 L. R. A. (N. S.) 1100, 84 C. C. A. 553)), the doctrine is explained as resting upon a 'fiction'. *But whatever name be given to it, the rule originates in and rests upon the underlying presumption 'that a person is innocent of crime or wrong.'* (Code Civ. Proc., sec. 1963, subd. 1.)

"Has the doctrine any proper application to a case, like this, where a party has fraudulently induced another to enter into a contract, and holds what he has received thereunder in trust, not by virtue of any contractual or acknowledged fiduciary relation, but merely because the law declares that he is an involuntary trustee of property obtained by fraud? Is it to be presumed that one who has obtained property fraudulently under an agreement whereby it becomes his own (subject merely to the other party's right of rescission) will, notwithstanding his acquisition and holding under a claim of ownership, keep the property intact, for the benefit of the one from whom he has obtained it? *Can the wrongful act of the party obtaining the money furnish the basis for making him*

a trustee, and at the same time the ground for presuming that he acts rightfully? These questions have been directly presented to the supreme court of Iowa, which has answered them by saying that the rule relied upon by the appellant does not apply to involuntary trusts arising solely from fraud. In *In re* First State Bank of Corwith, 149 Iowa, 662 (129 N. W. 70), that court said: 'While we have held that where a bank receives money wrongfully, a trust arises as between it and the true owner of the money, we have never held that the wrongful act of the bank will alone create a preference as against general creditors, Are the appellees herein entitled to the aid of the legal presumption that their money reached the hands of the receiver in the form of increased assets of the bank, and that it may be taken therefrom without impairing the rights of the general creditors? *We are of the opinion that an affirmative answer to the inquiry would require us to go a step further than we have ever gone, and to establish a rule that would be unjust and inequitable.* . . . In all of our cases, except one which will be noticed later, where the presumption has been given force, the deposits were of trust funds, the character of such funds was known to the banks when the deposits were made, and the deposits involved no wrongful act on the part of the banks. *The presumption was in every instance based on the theory that the bank, knowing the character of the fund and acting honestly, would not use or dissipate it as long as it had funds of its own.'* The court then goes on to explain Whitcomb v. Carpenter, 134 Iowa 227 (10 L. R. A. (N. S.) 928, 111 N. W. 825, the exceptional case to which it had referred, by saying that the bank had there become a trustee by contract. 'But in any event,' continues the opinion,

'we do not think that it can be presumed that a bank will keep money that it has obtained by means of wilful and deliberate criminal acts. The ordinary thief disposes of stolen property as soon as possible, and it would be going a long way to say that a bank that has obtained money by means of its deliberate forgery will be presumed to have kept it on hand to be returned to the injured party intact. We are not willing to so hold, and without such presumption the appellees have made no showing that entitles them to preference.'

"The appellant is not correct in his statement that the case just cited has been overruled. On the contrary, it has been approved in a later decision by the same court. (In re First State Bank, 152 Iowa 724 (133 N. W. 354).) Nor are we cited to any authorities holding the contrary. In re Hallett's Estate, L. R. 13 Ch. Div. 696, a leading case, is relied on by the appellant. It does not, however, hold that the presumption applies to cases like the one before us. It merely holds that it is applicable not merely to the technical relation of trustee and *cestui,* but to all relations of a fiduciary character, as, for example, that of principal and agent. In all of the other cases cited, the money in question was either received in trust or was taken from a trustee with notice of the character in which he held it.

"There is, of course, no pretense that petitioner has traced, or can trace, his twelve thousand dollars into the possession of the receiver, except by means of the artificial presumption or fiction upon which he relies. *The controversy, in its essence, is between the petitioner and other claimants whose only recourse is to a fund insufficient to meet the demands upon it. All*

> *concerned must suffer some loss through the mismanagement or misconduct of the officers of the bank." People v. Calif. Safe Dep. & Trust Co.* (1917), 175 Cal. 756, 759, 760-762.

Even in the case of *Knatchbull v. Hallett, supra,* which is the foundation of the "low balance" presumption, the distinction between ordinary fiduciaries and a trustee *ex maleficio* was recognized. Contrary to the statement in the opinion of this Court, no tort feasor was involved in the English case. Baggallay, L. J., expressed the view in the English case that since the low balance theory was based on a fiction of honesty, it could be rebutted, and would be rebutted by proof of dishonesty such as that the funds were improperly taken in the first instance, or that the trust was repudiated as would be shown by a drawing of the total in the account below the amount of the trust funds. *Knatchbull v. Hallett,* 13 Ch. Div. 696, at 743.

The case of *Mitchell v. Dunn* (1930), 211 Cal. 129, 136, was a case involving a solvent trustee, and the court expressly recognized that it would indulge in presumptions against a solvent trustee which would be unwarranted against other creditors if the trustee were insolvent.

While the rule of property is established by the California Supreme Court for California property, we desire to call attention of this court to a few of the decisions of other courts which have refused to apply a "low balance"

presumption under circumstances similar to those existing in the *Richfield* case.

> *Rugger v. Hammond* (Wash., 1916), 163 Pac. 408;
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> *Philadelphia Nat'l Bank v. Dowd* (C. C. N. C., 1889), 38 Fed. 172;
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> *Poole v. Elliott* (C. C. A. 4, 1925), 76 Fed. (2d) 772, 774, 775;
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> *Stilson v. First State Bank* (Ia., 1910), 129 N. W. 70, 72, 73;
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> *American Employers' Inc. Co. v. Maynard* (Mich., 1929), 226 N. W. 686.

It is of course obvious that if Universal had no property interest in the bank account of Richfield at the time the checks were drawn on that account to make the investments which are the subject of this proceeding, Universal could not possibly trace any property interest into the investments themselves. It is equally obvious that upon the application of the above rule of property established by the California Supreme Court and the facts adduced in this case, Universal established no property interest in the bank account of Richfield at the time any of the investments in question were made. The facts in evidence show that in every instance the amount checked against the account, between the time each deposit of Universal funds was made in the account of each such deposit of Universal funds. The following is a schedule of said facts in evidence:

Date of Deposit	Amount of Deposit	Closing Balance	Date of first subsequent disbursement for properties sought to be traced	Total disbursements from the account between two dates immediately to the left
Nov. 13, '29	$750,000.00	$2,417,148.32	Nov. 29, '29	$5,074,049.65
Jan. 20, '30	200,000.00	1,242,607.82	Jan. 27, '30	1,795,588.66
Feb. 15, '30	500,000.00	1,128,227.19	(Next deposit) Feb. 25, '30	2,705,967.54
Feb. 25, '30	100,000.00	252,760.24	(Next deposit) Feb. 27, '30	48,621.95
Feb. 27, '30	100,000.00	608,346.67	Mar. 1, '30	222,073.94
June 6, '30	75,000.00	216,959.33	June 25, '30	3,347,662.88

Referring to the above schedule it appears that on November 13, 1929, the first deposit of so-called "trust funds" from Universal was made in the general account of Richfield with Security-First National Bank of Los Angeles. At the close of that same day, due to other funds of Richfield being in the account, the balance in the account was $2,417,148.32. Between that time and the opening of the account on November 29, 1929, the date the first disbursement was made for the properties sought to be traced, there had been disbursed from the account $5,074,049.65, even without taking into account additional checks charged to the account on Nov. 13, 1929, after the deposit in question. Counsel for Universal on these facts ask the court to find that they have proved that the $750,000 in trust money did not go out with said disbursement of $5,074,049.65, but through some fortuitous circumstances still remained in the account, at least to the extent of the lowest balance of the account between November 13 and November 29. Such proof would, of course, be no proof at all but would merely be dispensing with proof in the guise of a fiction or presumption, which under the circumstances of this case *and under the decision of the Supreme Court of California* does not exist. Without the aid of such fiction or presumption as a substitute for

proof, it will be seen from the schedule immediately preceding that Universal has not shown that a single dollar of the trust funds was in the account at the times any of the disbursements therefrom sought to be traced were made.

It is of course true that if state court decisions attempt to create preferences and priorities without any tracing, the state rule is one of preference rather than of property, and the federal decisions on general equity jurisprudence are controlling as to preference in receiverships.

> *John Deere Plow Co. v. McDavid* (C. C. A. 8, 1905), 137 Fed. 802, 812;
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> *Beard v. Independent District of Pella City* (C. C. A. 8, 1898), 88 Fed. 375;
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> *Elmer v. Kemp* (C. C. A. 9, 1933), 67 Fed. (2d) 948, 952.

But the question of whether or not a trust interest under given facts actually exists on certain real or personal property is a question of property law. For example, since the tracing of a trust *res* is a matter of property right rather than debt, the California Supreme Court has permitted a *cestui* to recover funds from a mixed bank account of a decedent although the *cestui* had not filed a claim against the estate within the proper time to recover on a debt. *Noble v. Noble* (1926), 198 Cal. 129.

The question of whether a *cestui* has an interest in real or personal property is so clearly a question of property that it is cognizable by the state courts, even in the case of an insolvent national bank. If it were a matter of

preference rather than of property rights, the federal courts would have exclusive jurisdiction under a national bank receivership. *Davis v. Elmira Savings Bank* (1896), 161 U. S. 275, 283-4, 288-290. Nevertheless, on a question of the actual tracing of trust funds, this being a question of local property rights, state courts have jurisdiction even in the case of the insolvency of national banks. *Capital National Bank of Lincoln v. First National Bank of Cadiz* (1899), 172 U. S. 425, 432-433. In the latter case a state court decided that certain funds in the hands of a receiver of a national bank had been traced as trust funds. The court distinguished this from the case of a preferred claim, held that no federal question was involved, and upheld the jurisdiction of the state court to decide the point, saying:

> "The contention of plaintiff was that the Capital National Bank had money in its hands which belonged to plaintiff, did not belong to the bank, had never formed part of its assets, and was held by the bank in trust for plaintiff.
>
> "The right to the money was considered by the trial court in the light of general equitable principles applicable on the facts, and the court adjudged that the money constituted a trust fund to which plaintiff was entitled.
>
> "The decision did not purport to affect the assets of the bank, or attempt to direct the distribution thereof, or in any way to interfere with the disposition of assets actually belonging to the bank; nor did it affect the receiver as receiver; or his appointment or authority under the banking act. As the trial court found that certain moneys held by the bank in trust for plaintiff had come into the receiver's hands, he

was directed to return them, for he had no stronger title to the trust fund as against the plaintiff than the bank had.

"* * * it is clear that the state courts had jurisdiction to determine whether this money was or was not a trust fund belonging to plaintiff." Capital Nat. Bk. of Lincoln v. First Natl. Bk. of Cadiz, 172 U. S. 425, 432, 435.

While the last two cases cited from the United States Supreme Court are with respect to the jurisdiction of a state court, they clearly distinguish between a preference in receivership as a mere principle of equitable jurisdiction and a tracing of trust funds as a property right, which is a matter of local property law.

It is submitted that all questions of local property rights, both with respect to real and personal property, are governed by the decisions of the highest court of the state in which the property is situated, even when the case is in the federal courts.

Edward Hines Yellow Pine Trustees v. Martin, 268 U. S. 458, 464; 69 L. Ed. 1050, 1053 (1925);

Scandinavian-American Bank v. Sabin (C. C. A. 9, 1915), 227 Fed. 579, 582;

Pickens v. Merriam (C. C. A. 9, 1915), 274 Fed. 1, 8;

Jones v. Harrison (C. C. A. 8, 1925), 7 Fed. (2) 461, 464; Cert. den. 270 U. S. 652.

As succinctly said in Vol. 6, *Hughes Federal Practice*, section 3712, pp. 238-9:

"In considering generally the question whether or not the decisions of the state courts are binding on

the federal courts, reference was made to matter decided relating to local property rights, to the effect that when the thing decided in a state court relates to the acquisition, or not, of rights to, interest in, or liens upon, property located within the state, even though the acquisition, or not, depends solely upon the unwritten law of the state, the decision is to be followed in a federal court sitting in that state." Vol. 6, Hughes Federal Practice, Sec. 3712, pp. 238-9.

In *Edward Hines Yellow Pine Trustees v. Martin* (1925), 268 U. S. 458, 464; 69 L. Ed. 1050, 1053, the Supreme Court, in considering a bill in equity to remove a cloud on title to real property, said:

"To avoid the uncertainty and injustice which result from 'the discordant element of a substantial right, and which is protected in one set of courts and denied in the other, with no superior to decide which is right' (Brine v. Hartford F. Ins. Co., 96 U. S. 627, 24 L. Ed. 858), this court has not hesitated when there has been a conflict of decision between it and the state courts, affecting a rule of property within the state, to overrule its own decisions and to follow the state decisions once it has become evident that they have established a 'rule of property' as the settled law of the state (Green v. Neal, 6 Pet. 291, 8 L. Ed. 402; Suydam v. Williamson, 24 How. 427, 16 L. Ed. 742; Fairfield v. Gallatin County, 100 U. S. 47, 25 L. Ed. 544; Roberts v. Lewis, 153 U. S. 367, 376, 38 L. Ed. 747, 750, 14 Sup. Ct. Rep. 945; and see Bauserman v. Blunt, 147 U. S. 647, 37 L. Ed. 316, 13 Sup. Ct. Rep. 466, overruling a decision of the circuit court ante-dating a conflicting decision of the state court). We, are, therefore, constrained in the present case to accept the view of the state courts as

> announced by them without inquiring, as an original proposition, into the justice and sufficiency of the rule which we follow." Edward Hines Yellow Pine Trustees v. Martin, 268 U. S. 458, 464; 69 L. Ed. 1050, 1053.

In this respect there is no distinction between real and personal property, for, as said in 6 *Hughes Federal Practice,* section 3715, p. 248:

> "The decisions of the state courts as to personal property are rules of property, as are those involving realty, to be followed by the federal courts." 6 Hughes Federal Practice, section 3715, p. 248.

In *Scandinavian-American Bank v. Sabin* (C. C. A. 9), 227 Fed. 579, 582, the Circuit Court of Appeals for this circuit said:

> "In determining the validity of chattel mortgages in bankruptcy proceedings, the federal court will follow the settled law of the state in which the transaction occurred." Scandinavian-American Bank v. Sabin (C. C. A. 9), 227 Fed. 579, 582.

In *Pickens v. Merriam* (C. C. A. 9, 1915), 274 Fed. 1, 8, the question was whether real property in Kansas which the deceased had contracted to sell before his death was to be regarded as real property going to his widow, or as personal property divisible between his widow and other claimants. The Circuit Court for this circuit said:

"It is stated by Judge Story in his work on Equity Jurisprudence (volume 2, par. 1107):

'It is the exclusive province of the courts of the state of the situs of the property to determine its ownership, and its devolution to transfer, and whether or not there has been a conversion of the property from one sort to another. This is essentially so from the very nature of things, or else the state would have certain classes of property within its boundaries completely subject to the caprice and desires of non-residents, and thus render nugatory its laws enacted for the purpose of protecting its own citizens and their property rights.'

"That the decisions of the Kansas Supreme Court have established a rule of property as respects contracts of the kind involved here can scarcely be disputed. The construction of the contract given in the Pickens Case, *supra,* seems to have been first announced in Douglas County v. U. P. Ry. Co., 5 Kan. 615, 621, and has since been consistently followed. Brown v. Thomas, Sheriff, 37 Kan. 282, 15 Pac. 211; Drollinger v. Carson, 97 Kan. 502, 155 Pac. 923.

"These considerations lead to the conclusion that these contracts of sale did not work an equitable conversion of the real property concerned; that in their legal status, in view of the construction given them by the Kansas Supreme Court, they were properly to be considered and treated as real property, in the hands both of the vendor and his estate; and that they were rightfully so regarded in the administration and settlement of the estate. This disposes of the $22,-965.75 item. The complainants could have no right, title, or interest therein." Pickens v. Merriam (C. C. A. 9), 274 Fed. 1, 8.

In *Jones v. Harrison* (C. C. A. 8, 1925), 7 Fed. (2d) 461, 464, certiorari denied under name *Jones v. Readey*, 270 U. S. 652, the court said that as between the English rule restricting spendthrift provisions in trusts and the American rule which permitted such provisions to be more often enforced against attaching creditors, the state decisions should govern, saying "Whether the American rule shall be applied to equitable interests under a trust is a local rule of property binding on federal courts."

It is respectfully submitted that the California Supreme Court decision is binding upon and must be followed by the federal courts. Under that decision, and under the facts of the instant case, Universal had no property interests in the bank account of Richfield at the time the investments were made. The trust having failed at that time, there is no possibility of tracing any trust funds into the property purchased with checks drawn on the bank account thereafter.

IV.

Under the Circumstances of This Case, When Funds of a Cestui Are Comminged in a Single Bank Account With Funds of the Tortfeasor Trustee and Investments Are Later Made From Said Bank Account, the Cestui Cannot Claim Any of Such Investments at the Expense of the Other Creditors Against the Trustee's Insolvent Estate Unless the Cestui Sustains the Burden of Proving (1) That Trust Funds Remained in the Account at the Time the Investment Was Made; and (2) That the Trust Funds So Remaining in the Account Were in Fact (and Not Merely Presumptively) Appropriated for the Purpose of Making the Particular Investment. It Is Submitted That Universal Has Not Sustained the Burden of Proof With Respect to Either of These Elements.

It is submitted that under point III of this petition, the authorities cited demonstrate that the established rules of property of California applicable to this case necessarily deny to Universal any interest in the bank account at the time the investments which are the subject of this proceeding were made. But in addition thereto, under the well-established principles adopted by the United States Supreme Court and the great weight of authority of other courts in this country, a *cestui* must prove that trust funds in a commingled account were intentionally appropriated to a particular investment before the *cestui* can claim that investment or any interest therein as against

creditors of the trustee, and Universal equally failed to introduce any evidence on this essential element.

Peters v. Bain (1889), 133 U. S. 670;

Ex Parte Schuyler, Chadwick & Burnham In re A. O. Brown & Co. (D. C. S. D. N. Y. 1911), 189 Fed. 432, 433-435. Reversed under name *In re A. O. Brown & Co.* (C. C. A. 2, 1912), 193 Fed. 30. Reversal by C. C. A. affirmed under name *Schuyler v. Littlefield* (1914), 232 U. S. 707, 58 L. Ed. 806;

Ex Parte First Nat. Bank of Princeton in re A. O. Brown & Co. (D. C. S. D. N. Y. 1911), 189 Fed. 432, 437-439. Affirmed under name *In re Brown* (C. C. A. 2, 1912), 193 Fed. 24. Affirmed under name *First Nat. Bk. of Princeton v. Littlefield* (1912), 226 U. S. 110;

Ferris v. Van Vetcher (1878), 73 N. Y. 113;

Board of Com'rs of Crawford County v. Strawn (C. C. A. 6, 1907), 157 Fed. 49;

Bright v. King (1898 Ky.), 20 Ky. Law Rp. 186;

Bevan v. Citizens National Bank of Lebanon (Ky. 1893), 19 Ky. Law Rep. 1261;

In re City Bank (D. C. Mich. 1910), 186 Fed. 413;

Gianella v. Momsen (Wis. 1895), 63 N. W. 1018;

Burnham v. Barth (Wis. 1895), 62 N. W. 96;

Standish v. Babcock (1894), 50 N. J. Eq. 628;

City of Spokane v. First National Bank of Spokane (C. C. A. 9, 1895), 68 Fed. 982;

Empire State Surety Co. v. Carroll County (C. C. A. 8, 1912), 194 Fed. 593, 605.

In the leading case in this country on the subject of tracing investments from commingled funds, *Peters v. Bain* (1889), 133 U. S. 670, we find facts very similar to those in the instant case except that they were more favorable to the *cestui,* both in the matter of the unfairness which gave rise to the trust and in the matter of the relative amounts of the trust moneys and the trustee's personal funds. In that case a brokerage firm had been organized in 1865 with a capital of $5,000, which was never increased. The brokerage firm obtained control of the bank in 1870 and proceeded to make use of the bank's funds for the firm's purposes, taking $1,443,462.99. Both the brokerage firm and the bank went into liquidation. The brokerage firm had purchased some assets directly with the funds of the bank. The court held that such of these assets as came to the assignee of the brokerage firm, called in the decision "properties of the first class", were impressed with a trust in favor of the bank. However, the court held that with respect to assets purchased with the general funds of the firm, with which had been mingled the bank's funds, called "properties of the second class", no trust could be allowed, saying:

> " 'The property in the second class, however, occupies a different position. There the purchases were made with moneys that cannot be identified as belonging to the bank. The payments were all, so far as now appears, from the general fund then in the possession and under the control of the firm. Some of the money of the bank may have gone into this fund, but it was not distinguishable from the rest. The mixture of the money of the bank with the money of the firm did not make the bank *the owner of the whole.* All the bank could in any event claim

would be the right to draw out of the general mass of money, *so long as it remained money,* an amount equal to that which had been wrongfully taken from its own possession and put there. Purchases made and paid for out of the general mass cannot be claimed by the bank unless it is shown that its own moneys *then* in the fund were *appropriated for that purpose.* Nothing of the kind has been attempted here, and it has not even been shown that when the property in this class was purchased, the firm had in its possession any of the moneys of the bank that that could be reclaimed in specie. To give a *cestui que trust* the benefit of purchases by his trustees, it must be satisfactorily shown that they were *actually* made with *trust funds.'"* *Peters v. Bain* (1889), 133 U. S. 670, 678.

Reiterating in a later part of the decision:

"'Purchases made and paid for out of the general mass cannot be claimed by the bank, unless it is shown that its own moneys *then* in the fund were *appropriated* for that purpose. And this the evidence fails to establish as to any other property than that designated in this decree.'" *Peters v. Bain* (1889), U. S. 670, 694.

It should be noted that this language of the United States Supreme Court succinctly states the necessity for the elements herein designated "1" and "2" for the tracing of investments from commingled funds, to-wit: that trust funds must be shown to have been in the commingled funds at the time the investment was made, and further that it must be shown that the disbursement made from the commingled fund was intended by the trustee as an appropriation of trust funds for such disbursement.

The *cestui* might show direct appropriation of trust funds from the bank account to a particular investment by evidence of different sorts such as (1) evidence of the similarity in the amount of trust funds in the account and the amount invested, as suggested in *Ferris v. Van Vechter* (1878), 73 N. Y. 113; (2) statements of the trustee to the effect that he was appropriating trust funds for a particular investment, as in *Moore v. Jones* (1883), 63 Cal. 12 and *Taylor v. Morris* (1912), 163 Cal. 717; (3) by "direct evidence" of the appropriation, probably by entries on the books of the trustee, as in *Fiman v. State of South Dakota* (C. C. A. 8, 1928), 29 Fed. (2) 776; or (4) by evidence that the whole balance of the account, which balance included trust moneys, was invested in a single property, as in *In re A. O. Brown & Co.*, D. C. S. D. N. Y., 189 Fed. 432.

The authorities which are cited in support of the contrary rule do not establish the principle for which they are cited. *Primeau v. Granfield* (D. C. N. Y., 1911), 184 Fed. 480, was a case of a solvent trustee, and as is abundantly pointed out in the authorities, the court is warranted in making almost any assumptions or presumptions it wishes in order to make the *cestui* whole at the expense of a defaulting trustee, where other creditors are not involved. The case of *In re A. O. Brown & Co.* (D. C. N. Y.), 189 Fed. 433, is discussed *supra*. The portion about tracing investments merely held that if trust funds are included in the balance of a commingled account, and all of the balance of the commingled account goes into a single investment, the trust funds must necessarily be included in the investment. The case of *In re Pacat Finance Corp.* (C. C. A. 2, 1928), 27 Fed. (2) 810, 814, has the elements of a

proved appropriation of trust money on direct evidence, and furthermore, the real basis of the decision is the fact that the court regarded the lire credits as cash in the bank, stating that the principle against restoration of a low balance by subsequent deposits "does not apply to cash in bank, and lire credits we regard as of that class". The court did cite *In Re Oatway,* but that citation was unrelated to the principles upon which the court decided the case and entirely unnecessary to its decision. In *Fiman v. State of South Dakota* (C. C. A. 8, 1928), 29 Fed. 2d 776, there was obviously, as the court found, "direct evidence" of the appropriation of the trust funds for deposit in the correspondent banks. There was no contested issue on this point, and undoubtedly there were entries made on the books, or some such evidence of the actual appropriation of trust moneys. In any event, the court's decision expressly rests upon the "direct evidence" of appropriation, and not upon any presumption. *Brennan v. Tillinghast* (C. C. A. 6, 1913), 201 Fed. 609, must either be considered as contrary to the great weight of authority, as it is according to the language of the opinion, or as being one of those numerous cases holding that all of the "cash items" of a bank, including cash in its vaults and that on deposit with correspondents, is to be considered as a single fund. This is the one federal case in insolvency proceedings which purports to follow the supposed rule of *In re Oatway.*

So much has been made of the case *In re Oatway* (L. R. 1903), 2 Ch. Div. 356, that a discussion of the same at this time, we believe, would be very profitable. That was a case of a creditor's action for the administration of the estate of Louis J. Oatway, a solicitor, who died

insolvent in 1902. The testator Oatway died with one thousand shares of the stock of Oceana Company standing in his name, which were thereafter sold for 2474£/19s. The issue was over title to these proceeds. Oatway and Skipper had been co-trustees under a will. They advanced 3000£ to Skipper in breach of the trust upon the security of a mortgage. On August 15, 1901, Oatway sold the property as mortgagee and also under a power of attorney which he held from Skipper, realizing 7000£ upon the sale. At that time Oatway had 77£/13s/4d in his personal account and deposited the 7000£ therein. On August 24, 1901, Oatway purchased the shares in question for 2137£/12s/3d, having since August 13, 1901, made deposits in the account of some 30£ and having drawn out of the account some 510£. After August 24, 1901, the balance of the account was dissipated. Skipper, on August 15, 1901, was indebted to Oatway in the approximate sum of 1779£ and also in further unascertained amounts. The proceedings are brought by Skipper to have the proceeds of the stock paid to him, *either in his personal capacity because of the 4000£ received by Oatway on the sale over the amount of the mortgage or as trustee to replace the 3000£ lent.*

The contention of counsel for Skipper was that the entire 7000£ were trust funds, that Oatway had first to replace the 3000£ and had to account to Skipper for the balance of 4000£, but counsel stated that Skipper did not desire to press his personal claim to the proceeds of the shares provided the trust was given the benefit of them, he to be relegated to recover against Oatway's estate. The court stated that Skipper, who was himself a party to the original breach of trust, could not under the cir-

cumstances, and in fact did not, oppose the claim of the trust to the proceeds of the Oceana shares, so that for the purposes of the case it was considered that Oatway was entitled to the balance of the 7000£ after discharging the 3000£ mortgage. The court held that the fact that the account still contained enough to discharge the trust at the time the shares were bought would not prevent the trust from having a claim on the shares when the balance of the account was dissipated. It is submitted that the decision is only applicable to the peculiar facts of that case. The trust had had a lien upon the Skipper property which had been mortgaged. The proceeds from the sale of that mortgage were deposited in an account in which only a very small amount of the trustees' own personal funds were deposited. The investment was made nine days after the deposit, at which time very little had been withdrawn from the account, so that the requirement that the trust funds be shown to be in the account at the time of the investment was satisfied. Skipper's counsel evidently did not concede that the balance of the sales money belonged to Oatway. Rather, he contended that Oatway was obligated to him for the balance of such sales price, but was willing to waive his claim to the proceeds of the shares provided the trust got the benefit thereof. It is highly probable that the entire 7000£ were trust moneys for two different *cestuis,* one of whom has waived his claim provided the other is given the investment. If the entire 7000£ was a trust fund, even though one *cestui* waived his rights provided the other were given the investment, the investment was necessarily made from trust funds. In any event, *since* the decision of *In re Oatway* the United States Supreme Court has announced

a diametrically opposed rule under facts similar to those surrounding the Universal claim.

In *Schuyler v. Littlefield* (1914), 231 U. S. 707, 58 L. Ed. 806, the court was very specific in saying that there must be evidence of the appropriation of trust money from a commingled account to a specific investment before there can be a tracing into that investment. In the case below in the Circuit Court of Appeals, Second Circuit, *In re A. O. Brown & Co.,* 193 Fed. 30, 33, the claimant had traced his funds into an indebtedness owed the bankrupt, which indebtedness was paid to the bankrupt on August 24, in two checks. The smaller check was deposited on the 25th and was held to have been dissipated. The larger check was deposited on the 24th, and claimant asserted that if the proceeds of his stock were in the larger check it went out in the check used to pay off a specified secured loan on that day, and that he should be entitled to a lien on the collateral released by this payment. The federal courts have always held that if trust funds could be traced into payment of a secured loan, the *cestui* would have a lien on the security thus released, just as he would have on any other investment made with the trust moneys. However, the Circuit Court of Appeals denied the claimant's contention on two grounds: First, he had not shown that the larger check in which he claimed his funds were included had been deposited in the bank prior to the payment of this particular secured loan, or any other secured loan; and second, that even if the so called larger check had been deposited before the payment of the secured loan, the claimant had produced no evidence that the trust moneys included in that larger check had been appropriated to pay off this particular

loan. In other words, the Circuit Court of Appeals refused to find that, merely because trust moneys were in an account the trustee, the *cestui,* could claim any investment made with funds from that account. This decision was affirmed by the United States Supreme Court in *Schuyler v. Littlefield, supra,* the Supreme Court saying that not only did the record fail to show when the larger check was deposited on the 24th, but

> "* * * it also fails to show with the requisite certainty the particular uses made by Brown & Co. of that money. The banking transactions on August 24th involved several millions of dollars * * *. Payments to the bank were made on account of notes, some of which represented loans appearing in the deposit account and others represented loans which had not been so entered. Some of the loans were secured and others were unsecured, and whether the money received from Miller (which included the trust fund of $9,600) was used to pay the secured or unsecured loans does not appear with certainty. * * *
>
> "They were practically asserting title to $9,600, said to have been traced into stock in the possession of the trustee. Like all other persons similarly situated, they were under the burden of proving their title. If they were unable to carry the burden of identifying the fund as representing the proceeds of their Interborough stock, their claim must fail. If their evidence left the matter of identification in doubt, the doubt must be resolved in favor of the trustee, who represents all of the creditors of Brown & Company, some of whom appear to have suffered in the same way. Like them, the appellants must be remitted to the general fund." *Schuyler v. Littlefield,* 232 U. S. 707, 713.

A careful reading of this case as it proceeded through the courts shows that there was no failure to identify the particular secured loan which it was alleged was paid with a check on the commingled account on August 24th. The Circuit Court of Appeals for the Second Circuit and the United States Supreme Court above held, however, that in addition to the failure of claimant to show that his moneys were in the account, he also failed to show whether the trust moneys went out in checks to pay secured loans (investments) or checks to pay unsecured loans (dissipation).

In the present case, Universal produced no evidence that its funds, if in that account, were specifically and expressly appropriated to any particular investment as distinguished from the countless checks which went out of the account to pay indebtedness on the part of Richfield. It is respectfully submitted that without such evidence of appropriation Universal has completely failed in tracing its funds into properties in the hands of the Receiver.

Conclusion.

In the instant case the only direct evidence of tracing was that on particular days checks were drawn on the Universal bank accounts and deposited in the Richfield general account. Whether Richfield was a debtor or trustee for these funds was a question not entirely free from doubt at the trial of Universal's claim, but we are accepting the findings of the Master in the trial court that it was a trust relationship. Based on this single

fact, the Court first presumes that regardless of the fact that on the average more money went through the Richfield account every week than the total amount of the Universal funds involved, the Universal funds would remain in the account to the extent of the low balance of that account. Second, because the means of ascertaining the low balance have failed, the Court presumes that the low balance did not fall below the overnight balances. Whether this is called *"prima facie* evidence" or placing the burden of proof on the Receiver, it is in essence dispensing with proof. Finally, the Court presumes that any investment made out of the account during the time that the twice presumed trust funds were in it were made with trust moneys. It is respectfully submitted that it must be apparent that granting a lien to Universal under such a series of presumptions is merely an improper preference under the guise of "tracing". As said of a *cestui* in the case of *In re A. O. Brown & Co.* (C. C. A. 2, 1912), 193 Fed. 30, 32, *"He cannot trace his money by a mere succession of presumptions."*

We should not lose sight of the fact that the federal court took over these assets of Richfield to prevent preferences by attachment, taking of possession, recording of judgments, or otherwise. The principal purpose of the proceeding was to insure an equality of distribution among all claimants against an estate which was not sufficient to pay them all in full. We submit that the Court should not permit sympathy for the hardships of one claimant to blind it to the meritorious claims of six thousand other claimants who have submitted their rights to the federal courts, all of whom had tremendous hardships thrust upon them by this gigantic industrial failure.

In carrying out the principles of equity receiverships, it should be borne in mind that the authorities establish the principle that in cases of doubt claimants should be kept on a basis of equality rather than the chance taken of giving to one claimant property which is not his own, at the expense of the rest. In the last analysis equality is the highest equity. Mr. Faries says in the conclusion of his brief *amicus curiae,* that the principles here contended for resolve all doubt in favor of the wrongdoer Richfield and the trustee of its bond indenture. Rather, they resolve certain doubts in favor of the Receiver representing the thousands of claimants against the estate. Both this Court and the United States Supreme Court have heretofore ruled that all such doubts must be resolved in favor of the Receiver.

Titlow v. McCormick (C. C. A. 9, 1916), 236 Fed. 209, 211;

Schuyler v. Littlefield, 232 U. S. 707, 713; 58 L. Ed. 806, 809.

Respectfully submitted,

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The undersigned solicitors and counsel for the above named Appellee, William C. McDuffie as Receiver of Richfield Oil Company of California, do hereby certify that the foregoing Petition for Rehearing is, in our judgment, well founded, and that it is not interposed for delay.

Henry F. Prince,

Homer D. Crotty,

Herbert F. Sturdy,

David P. Evans,

Solicitors for Appellee, William C. McDuffie as Receiver of Richfield Oil Company of California.